

DEC 17 1991

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In The
Supreme Court of the United States

October Term, 1991

ALLSTATE INSURANCE COMPANY,
an Illinois Corporation,

Petitioner,

v.

SAMUEL F. FORTUNATO,
Commissioner of Insurance of
The State of New Jersey,

Respondent.

Petition For A Writ Of Certiorari To The
Appellate Division Of The Superior Court Of The
State Of New Jersey

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Does the Due Process Clause of the Fourteenth Amendment permit a State to compel a company to take on new business against its will and at State-mandated rates, without first permitting judicial review of constitutional adequacy of those rates?

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**PETITION FOR A WRIT OF CERTIORARI
TO THE APPELLATE DIVISION
OF THE SUPERIOR COURT OF
THE STATE OF NEW JERSEY**

Petitioner, Allstate Insurance Company ("Allstate"),¹ prays that a writ of certiorari issue to review the judgment and opinion of the Appellate Division of the Superior Court of the State of New Jersey ("Appellate Division") entered in this action on May 20, 1991.²

OPINIONS BELOW

The Commissioner entered the challenged order (Appendix 1) without opinion. The Opinion of the Appellate Division (Appendix 2) is reported at 248 N.J. Super. 367, 591 A.2d 631 (1991). The New Jersey Supreme Court denied certification without opinion (Appendix 3).

JURISDICTION

The final judgment of the Appellate Division was entered on May 20, 1991. Allstate filed a timely petition for certification by the New Jersey Supreme Court on July 9, 1991 (App. 4). On July 12, 1991, Allstate also filed a timely notice of appeal as of right on the constitutional issues presented (App. 5). The New Jersey Supreme Court's denial of certification (which also dismissed the

¹ Allstate is a wholly-owned subsidiary of Sears Roebuck & Co. Allstate's non-wholly-owned subsidiaries are Allstate Automobile & Fire Insurance Company, Limited; Saison Life Insurance Company, Ltd.; Samshin Allstate Life Insurance Company, Ltd.; and Tramed (a Russian company).

² The respondents to this petition are Samuel F. Fortunato, Commissioner of Insurance of the State of New Jersey ("Commissioner"); Aetna Casualty & Surety Co. ("Aetna"); and Colonial Penn Insurance Company ("Colonial Penn"). Aetna and Colonial Penn were the subjects of orders similar to the one issued to Allstate, and the three appeals from those orders were consolidated.

appeal) was entered on September 18, 1991. Jurisdiction is conferred on this Court by 28 U.S.C. § 1257.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

This case presents questions under the Fifth and Fourteenth Amendments to the United States Constitution (App. 6). It implicates the following New Jersey statutes: The Fair Automobile Insurance Reform Act of 1990 ("FAIRA"); N.J. Stat. Ann. 17:29A-14 to -44, 17:29C-7.1, 17:30E-1 to -14, 39:6A-3; and N.J. Admin. Code 11:2-29.1 *et seq.*, 11:3-8.3 to -8.4. All are reproduced in Appendices 7 and 15.

STATEMENT OF THE CASE

Nature of the Case

The confiscatory order at issue in this case is the product of a long and sorry history of New Jersey regulation. That January 24, 1991 order ("Depopulation Order" or "Order") of the Commissioner requires Allstate to offer insurance for over 32,000 vehicles ("exposures") previously insured by state-run entities. *Under this Order, Allstate will be required to issue policies at rates which would produce an annual operating loss of over \$600 per assigned policy and over \$20,000,000 total.* (Aa 43A-44A, ¶ 3)³

Allstate could not recoup any of the losses on this assigned business in the New Jersey voluntary automobile insurance market, because suppressive rate regulation promises to produce an operating loss of over \$90 million on all of Allstate's New Jersey voluntary auto policies written in 1991. (Aa 44A, ¶ 5) Indeed, that same rate regulation had already caused Allstate \$32 million in

³ Allstate's Appendix in the Appellate Division will be cited as "Aa." Allstate's Appendix to its stay motion to the Commissioner, which was accepted as a supplement to the record by the Appellate Division, will be cited as "Asa."

auto insurance operating losses over the prior 15 years. (Aa 44A, ¶ 4) Nor could Allstate's other lines of New Jersey insurance business (and those of its affiliates) generate sufficient profits to cover the heavy flow of red ink in the auto lines. (Aa 44A, ¶ 6)

Allstate cannot increase the rates for either its own business or the assigned business without the Commissioner's prior approval. That approval cannot be obtained without lengthy rate proceedings,⁴ during which Allstate would suffer enormous losses on the assigned business. Yet, New Jersey law does not permit losses resulting from inadequate rates to be recovered through future rate increases. *In Re Elizabethtown Water Co.*, 107 N.J. 440, 449-51, 527 A.2d 354, 359-60 (1987); *In Re Industrial Sand Rates*, 66 N.J. 12, 23, 327 A.2d 427, 433 (1974). And Allstate could not even cease doing business in New Jersey without the Commissioner's permission, which it is now seeking to obtain.⁵

⁴ While Allstate had applications for voluntary-market rate increases pending long before this case was filed (Asa Tabs 12, 13), New Jersey has yet to provide even an initial decision on those applications. Allstate has been permitted certain small increases in its voluntary-market rates to account for rising price levels. As explained at 29-30 n. 26, *infra*, none of those rate increases can possibly provide any excess profits in the voluntary market to subsidize depopulation losses. Thus, no action on voluntary-market rates has mooted Allstate's claim here. Allstate's projections for its 1991 New Jersey business have not changed materially since this case was filed.

⁵ The New Jersey no-fault automobile insurance statute N.J. Stat. Ann. 39:6A-1 *et seq.* ("No-Fault Act") requires an insurer to renew automobile insurance policies unless the Commissioner consents to non-renewal. *Id.* 39:6A-3; 17:29C-7.1. The Commissioner consents only in very limited circumstances. N.J. Admin. Code 11:3-8.3 to 8.4. This consent is required even when an insurer seeks to withdraw from the state. *Sheeran v. Nationwide Ins. Co.*, 80 N.J. 548, 556-57, 404 A.2d 625, 631 (1979).

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These events are the culmination of twenty years of abusive rate regulation by the State of New Jersey in the face of skyrocketing costs of compensating automobile accident victims. Unwilling either to curtail benefits or to make motorists pay for them in full, the State has continually kept insurance rates below cost, in large part by exploiting the potential for interim confiscation inherent in a strict system of purely prospective prior-approval ratemaking. The effect has been to bleed insurers of income and assets generated in other States for the benefit of New Jersey motorists, first holding out the illusory hope of a brighter tomorrow, then obstructing exit by automobile insurers.

In 1983, when suppression of rates led insurers to curtail their voluntary New Jersey auto insurance business, the State created the New Jersey Automobile Full Insurance Underwriting Association (the "JUA") to insure, at standard-risk rates, those very motorists to whom insurers were unwilling to sell insurance voluntarily at those rates. There were supposed to be subsidies built into the system to cover the rate deficits sure

(Continued from previous page)

The Fair Automobile Insurance Reform Act of 1990 ("FAIRA") also prohibits withdrawal except pursuant to a detailed plan approved in advance by the Commissioner. FAIRA, § 72. The Commissioner ordinarily requires the insurer to continue writing automobile insurance for five years after he approves such a plan, during which an insurer must expand its New Jersey automobile insurance business as required by depopulation obligations and soon-to-be-effective obligations to write insurance on request for all "eligible" drivers. N.J. Admin. Code 11:2-29.1 *et seq.* (App. 15); FAIRA § 27(b).

Allstate filed a proposed plan of withdrawal on September 16, 1991. The Commissioner has requested additional information before he will act on that plan. On this basis, it appears that Allstate is unlikely to be able to cease doing business in New Jersey before 1997, and there is no assurance that it will be able to do so even then.

to result from selling JUA policies at standard rates. But the Commissioner, unwilling to force motorists to pay the full subsidy required, adopted "cash-flow" ratemaking techniques which postponed funding of losses into the future. When the inevitable crash came in 1990, the JUA was replaced by a new entity, the Market Transition Facility ("MTF"), and the lion's share of the \$3.3 billion JUA deficit was imposed on the insurance industry.

New Jersey now seeks to compel insurers to cover JUA/MTF risks at MTF rates, whose demonstrated gross inadequacy is the legacy of the deliberately inadequate JUA rates, while subjecting insurers to protracted rate proceedings during which their right to be free from confiscation receives no protection at all.

Allstate has shown *prima facie* that the Depopulation Order will have a confiscatory effect. Yet, both the Commissioner and the New Jersey courts have refused to provide procedures adequate to prevent such confiscation during the pendency of the protracted rate proceedings. Accordingly, Allstate submits that, on the record presented here, the Commissioner cannot require it to obey the Depopulation Order without first either providing the rate relief shown *prima facie* to be necessary or allowing Allstate to obtain judicial review of a decision that such relief is unnecessary.⁶

New Jersey's High Cost and Underfunded Automobile Insurance System

In 1972, New Jersey adopted a No-Fault Act designed to provide prompt benefits to all accident victims while

⁶ It should be emphasized that the rate relief which Allstate seeks (absent a finding of no confiscation) could be temporary, "interim" relief, escrowed until the final rate determination and refunded (with interest) if later found excessive. Thus, Allstate would be able to collect the rates eventually found necessary, while policyholders ultimately need never pay any excessive amount.

reducing or stabilizing automobile insurance prices. *Thermographic Diagnostics, Inc. v. Allstate Ins. Co.*, 125 N.J. 491, 508, 593 A.2d 768, 778 (1991). However, the No-Fault Act failed to balance benefit increases with sufficient cost reductions. It thus substantially increased losses payable by insurers.⁷

While New Jersey officials were unwilling to reduce the costs of the no-fault system enough to bring it into balance, they were equally unwilling to impose the entire cost of that system on the voting public. As Deputy Commissioner Grubb succinctly put it (Aa 56A):

Since 1973, New Jersey has used tight controls on auto rates to avoid paying the actual cost of the state's high accident rate and unbalanced no-fault system. As a result, the voluntary market has been unprofitable, and the residual market (ie., the JUA) has grown to almost half of the state's motorists.

This fact was confirmed by an *Insurance Profitability Report*, published by the New Jersey Department of Insurance in November, 1989, which found that "although private passenger auto has been a profitable insurance line nationally, the industry generated a 2.8 percent operating loss, or \$521 million, in New Jersey over a 13-year period ending in 1988." (Aa 47A)

As already shown, if an insurer's rates are inadequate, New Jersey law does not permit the resulting losses to be recovered through future rate increases. Yet all increases require the prior approval of the Commissioner, who has extensive power to delay or deny such increases even if well justified.

⁷ This fact was acknowledged by state officials, including then Governor Kean, *Governor's Reconsideration and Recommendation Statement to Senate No. 2637-L. 1988 c. 119*, reprinted at *N.J. Stat. Ann.* 17:28-1.4, and Special Deputy Insurance Commissioner David N. Grubb, in a 1988 report entitled *Solving the Auto Insurance Crisis in New Jersey* (the "Grubb Report"). (Aa 54A-56A)

To alter its rates, an insurer must file proposed amendments with the Commissioner and obtain his approval. *N.J. Stat. Ann.* 17:29A-14. The Commissioner can certify the filing for a hearing and is required to do so on request. *Id.* Until the Commissioner decides, the insurer has not exhausted its administrative remedies, and, so, is unable to obtain substantive judicial review. After a decision, judicial review of a denial or partial denial of the insurer's application normally consumes many months, if not years.⁸

In most lines of insurance, an insurer unable to obtain adequate rates could curtail its writings in the affected market or withdraw entirely. But, as noted at 3-4 n. 5, *supra*, that option is not available to New Jersey automobile insurers. Of course, insurers with a reasonable expectation of making an adequate return would not wish to leave. And New Jersey would not feel the need to erect ever higher barriers to exit unless it thought insurers in general were concerned with rate adequacy. In fact, a number of insurers had left New Jersey prior to the 1990 enactment of FAIRA, and there is now a virtual stampede. See *In the Matter of the "Plan for Orderly Withdrawal from New Jersey" of Twin City Fire Ins. Co.*, 248 N.J. Super. 616, 591 A.2d 1005 (App. Div. 1991). As previously noted, Allstate, having curtailed its writing for many years, now seeks to withdraw entirely from New Jersey.

The Rise and Fall of the JUA

Because the No-Fault Act required all motorists to maintain insurance, *N.J. Stat. Ann.* 39:6A-3, some mechanism was necessary to provide coverage to those unable

⁸ Allstate has pending rate requests filed in August and October, 1990. Hearings on the latter filing are complete, and a decision by the Administrative Law Judge is required by early 1992, with a decision by the Commissioner due a few months later. The earlier filing is mired in discovery, and no hearing has yet been scheduled.

to obtain it in the voluntary market.⁹ The Act called for an "assigned risk" plan through which high-risk motorists could be assigned to insurers at rates established by the plan. *N.J. Stat. Ann.* 17:29D-1. The assigned-risk rates were based largely on state-regulated voluntary-market rates for standard risks. Beginning in the 1970's, the Commissioner provided some subsidy to the assigned risk rates by including certain "flat charges" or "policy constants" in premium rates for all policies (including those in the voluntary market). See *State Farm Mutual Auto. Ins. Co. v. State*, 124 N.J. 32, 41-42, 590 A.2d 191, 196 (1991).

The New Jersey Automobile Full Insurance Availability Act of 1983 ("the JUA Act"), *N.J. Stat. Ann.* 17:30E-1 *et seq.*, abolished the assigned risk plan and created the JUA to insure those unable to procure coverage in the voluntary market. The JUA was to function as an entirely independent insurance company; private insurers were to have no liability for JUA policies. *N.J. Stat. Ann.* 17:30E-7(b), -8(a). *State Farm Mutual Auto. Ins. Co. v. State*, 124 N.J. 32, 41, 590 A.2d 191, 196 (1991). The JUA had no capital, so it was crucial that JUA revenues be adequate and proper reserves be maintained (notably for losses which had already occurred but had not yet been adjusted and paid). The Commissioner had "plenary powers" to set policy for the JUA and control its operations. *Id.*

The Legislature contemplated that JUA rates would be similar to those for standard risks in the voluntary market, and, so, would not suffice for higher-risk JUA policies. *State Farm Mut. Auto. Ins. Co. v. State*, 124 N.J. 32, 41-42, 590 A.2d 191, 196 (1991). Accordingly, it provided

⁹ Ordinarily, even relatively high risks are voluntarily insurable if insurers are able to charge a premium adequate to reflect the risk. However, if they are prevented from charging an adequate rate, as has often been the case in New Jersey, or the insured is unwilling or unable to pay it, even a low-risk insured may be frozen out of the voluntary market.

the JUA with additional sources of revenue: policy constants collected on voluntary-market policies and certain Department of Motor Vehicles surcharges collected from those with bad driving records. *N.J. Stat. Ann.* 17:30E-8(a); 17:29A-35. The Commissioner was also empowered to impose a residual market equalization charge ("RMEC") to be collected by insurers on every insured vehicle and remitted to the JUA. The RMEC was to be set to allow the JUA to operate on a no-profit, no-loss basis. *N.J. Stat. Ann.* 17:30E-3(o), 8(b).

The JUA Plan of Operation was to provide, *inter alia*, "methods and standards for the establishment of adequate and actuarially sound reserves for unpaid losses, including provisions for incurred but not reported losses." *N.J. Stat. Ann.* 17:30E-6, -7(r). Regulatory insurance accounting requires that amounts reserved or added to reserves be treated as expenses in calculating profit or loss. Thus, to operate on a no-profit, no-loss basis, the JUA required a RMEC on voluntary-market policies sufficient (with other JUA revenues) to fund the necessary reserves. The JUA Plan, as approved by the Commissioner, initially required the JUA Board to recommend a RMEC computed on this basis. (Aa-231A-235A)

In 1984, the JUA Board recognized that the JUA was operating at a loss and recommended a RMEC for 1985 to meet the aforementioned statutory mandate to balance its books. However, rather than approve a RMEC for 1985 – a gubernatorial election year – the Commissioner mandated that the JUA adopt a cash-flow method of accounting, paying claims arising out of old policies with premiums received under new policies *without* setting aside the reserves necessary to meet the obligations arising under the policies whose premiums were thus diverted. (Aa 237A-243A)

Adoption of cash-flow funding for the JUA made an eventual financial disaster virtually inevitable. Without reserves for losses already incurred, the JUA could not pay claims on policies already written unless it wrote more policies and then diverted the premiums received

on those new policies to satisfy the claims under prior policies. In other words, cash-flow underwriting made the JUA nothing more than a State-run Ponzi scheme.

The deterioration of the JUA's financial situation, caused by a prolonged freeze of its already inadequate rates, the refusal to implement RMEC's and the absence of reserves, ultimately put in jeopardy its ability to meet even its cash flow needs. In 1988, the Commissioner was finally forced to implement a RMEC. *State Farm Mut. Auto. Ins. Co. v. State*, 124 N.J. 32, 42, 590 A.2d 191, 196 (1991).

In 1988, the New Jersey Legislature sought to begin depopulating the JUA, then insuring roughly half of New Jersey's motorists (*id.*), by requiring the voluntary market to absorb those JUA insureds with better driving records. FAIRA § 20. Insurers were not to be allowed to charge rates which would make such drivers attractive customers, but compelled to take assigned quotas of JUA insureds, whether or not they were attractive. FAIRA § 20. FAIRA accelerated JUA depopulation and prohibited the JUA from issuing or renewing any policy after September 30, 1990. FAIRA §§ 16, 88(c)(5).

FAIRA created the MTF to arrange for the issuance and renewal of policies from October 1, 1990 through September 30, 1992.¹⁰ FAIRA § 88(a)-(c). The MTF was initially to charge the JUA rates in effect on September 30, 1990. FAIRA § 88(c)(2). *However, the MTF was to receive neither policy constants nor RMEC's, which had amounted to roughly a third of the JUA's revenues.* (App. 13 at 294) Loss of these subsidies alone required a 50% increase in JUA rates just to restore the revenue level which produced the

¹⁰ By September 30, 1992, the MTF is to be populated by no more than 10% of New Jersey drivers, with driving records so poor they will not be "eligible" for voluntary-market insurance. FAIRA § 88(c)(5). They are to be insured by a new assigned risk plan. FAIRA § 34. Effective April 1, 1992, all drivers legally "eligible" for insurance in the private market will be entitled to buy it from any insurer they choose. FAIRA § 24.

JUA deficit; more than 50% would be required to fund reserves for payment of current claims and thus attain a break-even level, even with no new or increased costs. The losses suffered by the MTF (or, hypothetically, its profits) were to be shared among the insurers doing business in the voluntary market. FAIRA § 88(a).

By the time it ceased writing policies, on October 1, 1990, the JUA had run up an admitted deficit of \$3.3 billion in seven years. *State Farm Mut. Auto. Ins. Co. v. State*, 124 N.J. 32, 43, 590 A.2d 191, 196 (1991).

Funding the JUA Deficit

Under FAIRA, funding to pay the \$3.3 billion in claims for which the JUA had accumulated no reserves is to come largely from a 5% tax on insurers' premium receipts for three years and assessments on insurers of \$160 million per year (2.7% of premiums in 1990) for eight years. *State Farm Mut. Auto. Ins. Co. v. State*, 124 N.J. 32, 43-45, 590 A.2d 191, 197 (1991). On the face of the statute, insurers are forbidden to recover those taxes and assessments from their policyholders. *Id.* The Commissioner, in defending attacks on this scheme, took the position that, as a matter of statutory construction, FAIRA taxes and assessments can be considered expenses for ratemaking purposes if that proves necessary to avoid an unconstitutional confiscation of insurers' property. The New Jersey Supreme Court accepted this construction to avoid facial invalidation of the statute and directed that the resulting rate filings be handled expeditiously. *Id.* at 58-63, 590 A.2d at 204-07. In practice, however, the Commissioner has – as usual – delayed dealing with these filings.

Based on the Commissioner's position, and even prior to the New Jersey Supreme Court's decision, in August 1990 Allstate made a rate filing seeking recovery of FAIRA taxes and assessments. In November, 1990, the Commissioner rejected that filing on the ground that it failed to comply with new procedures which he was

planning, but had not yet published or promulgated. *Allstate Ins. Co. v. Fortunato*, 248 N.J. Super. 153, 157-58, 590 A.2d 690, 692 (App. Div. 1991). Not surprisingly, the Appellate Division held that the filing must be accepted. *Id.*

The Appellate Division found the Commissioner's excuse for his dilatory conduct "lame indeed," and declared that "there must be an end to the delays in the Department's preparations to deal with its [statutory] responsibilities." *Id.* at 165, 590 A.2d at 696. It pointed out the severe

impact of delay on the insurers. Their surtax and assessment liabilities commenced with the enactment of the FAIR Act, and represented millions of dollars of new costs. If the insurers were entitled to pass those costs along, . . . they can do nothing without action by the Commissioner. Approval of a rate filing is prospective only. . . . Thus, the longer it takes the Commissioner to consider a filing, the greater are the permanently lost revenues, no matter how clearly entitled to them the insurers may ultimately be proven to be.

Id. at 160-61, 590 A.2d at 694 (citation and footnote omitted).

Neither the Commissioner nor the New Jersey Supreme Court has indicated any way by which, in light of the purely prospective nature of ratemaking, insurers can recover taxes and assessments paid prior to approval of the newly required filings. Thus, to avoid further potentially irrecoverable losses, Allstate sought permission to put its proposed increase into effect on an interim basis during the rate proceeding, subject to later refund if found unjustified. The Commissioner denied this request,¹¹ and Allstate is currently

¹¹ The Commissioner concluded that he lacked power to grant such interim relief, and that, even if he had the power, interim relief would be improper unless it were absolutely certain that Allstate would otherwise suffer confiscation – a standard which cannot possibly be met where the rate proceeding is incomplete and Allstate's contentions disputed. (App. 16) However, New Jersey clearly recognizes the general need for such relief, and the Commissioner has been permitted to

seeking judicial review of that denial. *In Re Allstate Ins. Co.*, No. A-6219-90T5 (N.J. Super. App. Div.). The rate proceeding itself is currently mired in discovery, by the Commissioner and the Public Advocate, and no hearing date has yet been set.

The MTF Rate Filing

By statute, the JUA's rates (but with no RMEC's and policy constants) became those of the MTF on October 1, 1990. FAIRA § 17. In November, 1990, the MTF obtained two independent actuarial studies indicating that its rates must increase an average of roughly 60% to cover the costs of insuring its current population. (Aa 187A-227A) In January, 1991, the Commissioner's deputy (to whom the Commissioner had delegated his sole authority to operate the MTF; see FAIRA § 88; App. 13 at 307) filed for an increase averaging only 28%. (Aa 140A-144A)

Filing for a rate increase substantially less than that necessary to cover the costs of insuring the MTF population seemingly meant that the remainder of the MTF's costs (amounting to hundreds of millions of dollars) would be imposed on Allstate and other private insurers, which are statutorily obligated to absorb the MTF's losses. FAIRA § 88; *but see* App. 13 at 304 (where the Commissioner deliberately incurs losses, he may not be able to require insurers to pay them).

The Proceedings Below

On January 24, 1991, while the MTF rate filing was pending, the Commissioner issued the Depopulation Order to Allstate (and similar orders to 44 other insurers).

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grant interim relief in circumstances where he found it desirable to do so. See *In Re Industrial Sand Rates*, 66 N.J. 12, 25-26, 327 A.2d 427, 434-35 (1974); *New Jersey State AFL-CIO v. Bryant*, 55 N.J. 171, 176-77, 260 A.2d 225, 227-28 (1969).

(App. 1) Allstate was ordered to issue policies at either its own voluntary-market rates or the almost-always higher MTF rates. Allstate promptly presented the Commissioner documentary evidence and declarations showing that compliance with the Order would have a confiscatory effect, and requested that the assignments be deferred until the Commissioner either provided rate relief or made judicially reviewable findings that no relief was necessary. (*Asa passim*; App. 8) The Commissioner did not respond, and the Appellate Division stayed the Order pending its decision.

With an exception not material here, the Appellate Division rejected statutory challenges to the Depopulation Order.¹² 248 N.J. Super. at 376-87, 591 A.2d at 636-41, App. 2 at 47-60; App. 9, 10, 11. It then reached Allstate's state and federal constitutional claim, beginning with the recognition that:

The insurers are entitled to earn a reasonable rate of return on their New Jersey auto insurance business. . . . There is . . . a right to have the regulatory agency which exercises the rate-making function do its job reasonably promptly, and

¹² The Appellate Division held that a statute forbade the Commissioner to require insurers to utilize or compensate JUA producers. 248 N.J. Super. at 380-83, 591 A.2d at 638-39; App. 2 at 55-56. This will allow insurers to use less expensive methods of providing policy service to assigned customers, but the savings would only minimally reduce the confiscatory effect previously projected.

To date, the Commissioner has not revised the order to delete the unlawful portion or to specify how policies will now be selected for assignment. Yet, the Commissioner's criteria indicating what types of policies are to be assigned were affirmed. 248 N.J. Super. at 378-80, 591 A.2d at 637-38; App. 2 at 49-51. So long as the Commissioner adheres to these provisions, alteration of the method of selecting individual policies of those types should not alter the economic impact of the order on Allstate. But until the Commissioner corrects the state law defect, Allstate has a temporary reprieve from the Order.

with no more delay than is necessarily involved in the review process itself. The prime reason for expecting prompt consideration of rate increases is that they are prospective only. Thus, rates that were inadequate during a prolonged review process can not be retroactively increased or otherwise made up.

Id. at 387, 591 A.2d at 642; App. 2 at 61 (footnote and citations omitted).

However, in light of the Commissioner's contention that his Order would not have a confiscatory impact, the Appellate Division found itself unable, on the current record, to determine which party was correct. The Appellate Division also noted that, just before its decision, the Commissioner had announced the grant of some rate relief to the MTF (without yet issuing a written order or opinion). Yet, despite the undisputed actuarial studies before it, the court felt unable to determine the impact of that increase. The court concluded that it was "in no position . . . to predict whether that untested new business taken on by the insurers from MTF at untested new MTF premium rates will result in future losses so clear and significant that the insurers are entitled to protection in advance." *Id.* at 390, 591 A.2d at 643; App. 2 at 64. It therefore granted no relief on Allstate's constitutional claims.¹³

The MTF Rate Increase

After the Commissioner's deputy filed for only a 28% MTF rate increase, Allstate sought leave to participate in the proceeding to urge the necessity of the 60% increase indicated by the two actuarial studies. The Commissioner denied that motion. (App. 12 at 291, 298)

¹³ Allstate then took an appeal to the New Jersey Supreme Court as a matter of right on the state and federal constitutional issues and sought discretionary review on one state statutory issue. As required, N.J.R. 2:12-9, all issues were presented in a single petition. (App. 4) The denial of certification had the effect of summarily dismissing the appeal. *Id.*

Ten days before the Appellate Division decided this case, the Commissioner announced an MTF rate increase of only 18.6%. (App. 12 at 284) He did not purport to find that an 18.6% increase would suffice to cover the costs of MTF insurance, and the record before him would not support such a finding.¹⁴

Six months later, on November 19, 1991, the Appellate Division (after expedited briefing) reversed the order denying Allstate an opportunity to participate in the rate proceeding, and remanded for expedited proceedings to set proper rates. It noted that the MTF had initially used JUA rates without the substantial subsidies provided to the JUA. (App. 13 at 294) Accordingly, the court found (App. 13 at 296-97) that

[i]t must have been apparent to the Commissioner, as the operator of MTF, that the JUA rates were too low. They were so low in the late 1980s that even cash-flow accounting, RMECs, bad-driver increases and other revenue enhancers did not prevent dramatic yearly deficits. The anticipated greater accountability and efficiency of MTF, limitation of generous policy benefits, and other cost containment measures could be expected to accomplish just so much. The loss of RMECs would be a tremendous loss of revenue, and there were no means provided in the FAIR Act to subsidize residual market premium rates.

* * *

Although the actuarial consultants both reported in the first half of November 1990 that MTF rates were grossly inadequate, the Special

¹⁴ Without the benefit of any contrary study, the Commissioner began by making various "adjustments" to the actuarial studies, which purportedly reduced the break-even rate from 60% to 47.4%. (App. 12 at 276-78, 284) He then identified factors which he claimed created some uncertainty as to the MTF's actual rate need, and simply declared that he would allow only an increase of 18.6%. (App. 12 at 284-89)

Deputy Commissioner of Insurance in charge of MTF did not ask the Commissioner for higher rates until January 17, 1991, when he formally submitted his "Filing for Rate Revision." The Commissioner studied the matter for another four months, and made his decision on May 10. MTF had by then been operating for more than 7 months with rates that were plainly and obviously too low.

The court then criticized the dubious basis for seeking only a 28% increase and the Commissioner's rationale (or lack thereof) for allowing only an 18.6% increase. (App. 13 at 297-301) Because the Commissioner had failed to provide adequate opportunities for Allstate and other interested parties to participate in the rate-setting process, the court remanded for further proceedings. It closed with this admonition (App. 13 at 309-10):

Rate hikes are prospective only. There is no way for MTF or voluntary market insurers to charge retroactively higher premiums for earlier policy periods. Thus, the continued inadequacy of MTF rates, if indeed they are inadequate, would constitute a continually increasing loss that could never be made up. In these circumstances, all practical speed is the only acceptable pace for appropriate proceedings for review and evaluation of MTF rates. It may not be possible to make definitive judgments about MTF's predicted losses, but there are enough problem indications to require the Commissioner's immediate attention.

In response to this order, the Commissioner's deputy filed, on December 4, 1991, a request for a 15% interim MTF increase, to take effect January 15, 1992.¹⁵

¹⁵ This filing, made by the Commissioner's deputy before the Commissioner, is a public record whose contents are judicially noticeable under New Jersey law. N.J.R. Evid. 9; *West Milford Twp. v. VanDecker*, 235 N.J. Super. 1, 11, 561 A.2d 607,

(App. 14) That request was based upon a new actuarial study.¹⁶

To cover the future costs of MTF risks, the study finds an increase with a probable range of 24% to 42% is needed, with a most probable need of 32.7%. It is possible that the needed increase might fall outside the probable range and be as low as 15% or as high as 50%. (App. 14 at 323) However, the study cautioned that these extreme figures have "*essentially zero credibility. . . . [and] [i]mplementation of a rate change less than the probable range would be . . . actuarially unsound and likely result in an MTF deficit.*" (App. 14 at 323 (emphasis in original)) Of course, the requested 15% increase is at the extreme low end of the possible range, a point of "essentially zero credibility."

Even a grant of the proposed 15% increase would not moot this case. Combined with the prior increase it would still not bring the MTF up to a break-even level according to *any* of the available evidence. As long as MTF business is apparently loss-producing, and there is no finding that Allstate has excess profits sufficient to absorb such losses, there is still a *prima facie* case that the Depopulation Order will have a confiscatory effect on Allstate.¹⁷

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612 (App. Div. 1989), *aff'd*, 120 N.J. 354, 576 A.2d 881 (1990). Factual statements therein are adoptive admissions by the Commissioner through his deputy. N.J.R. Evid. 63(8). Its contents are relevant to show that neither the 18.6% increase already granted nor the additional 15% increase now proposed moots this case.

¹⁶ The new study obtained by the Commissioner's deputy concluded that the MTF has already accumulated a deficit of roughly \$300 million, of which between \$50 million and \$147 million would have fallen on private insurers had they depopulated the MTF at the statutorily-required speed and charged MTF rates to the depopulated risks. (App. 14 at 314)

¹⁷ Adequate MTF rates would only prevent confiscation if depopulation assignments were an average or better sample of

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**REASONS FOR GRANTING THE WRIT
WHERE A STATE COMPELS A COMPANY
TO EMPLOY ITS PROPERTY FOR THE
PUBLIC SERVICE AT STATE-MANDATED
PRICES, IT MUST PROVIDE PROCEDURES
ADEQUATE TO PROTECT AGAINST ANY
UNNECESSARY RISK OF CONFISCATION
DURING THE PENDENCY OF PROTRACTED
PROCEEDINGS TO ADJUST THOSE PRICES.**

There is no question as to the substantive constitutional standards which govern rate regulation. Businesses required to provide public service – including insurers – must be allowed the opportunity to earn a just rate of return on their activities in the State. *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 310 (1989); *Helmsley v. Borough of Fort Lee*, 78 N.J. 200, 223, 394 A.2d 65, 70 (1978), *app. dismissed*, 440 U.S. 978 (1979).

Regulated rates must be sufficient not only to cover costs and expenses, but also to yield a profit “sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.” *Federal Power Comm’n v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944) (citations omitted). “[T]he return to the equity

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MTF risks. Unfortunately, under the Order this is not so. A statute prevents rates in any territory from exceeding statewide average rates by more than fixed percentages. *N.J. Stat. Ann.* 17:29A-36(c). Accident frequencies and other loss-producing factors in some territories exceed statewide averages by more than the statutory percentages. (Aa 73A) Thus, were MTF rates adequate, rates in lower-risk territories would have to be inflated to subsidize those in high-risk territories, producing a mix of overpriced and underpriced territories. With inadequate rates, all territories may be underpriced, but some are more so than others. Depopulation assignments are to be made disproportionately from those territories with the lowest percentages of drivers insured in the voluntary market. (App. 1 at 5-6) These are the most underpriced territories, which are least attractive to private insurers. As a result, depopulation risks are systematically underpriced relative to an average collection of MTF risks.

owner should be one which is commensurate with returns on investments in other enterprises having corresponding risks." *Id.*; *Hutton Park Gardens v. West Orange Town Council*, 68 N.J. 543, 570, 350 A.2d 1, 14-15 (1975). To force Allstate to suffer massive and unrecoverable overall losses resulting from involuntarily insuring depopulation risks would unconstitutionally confiscate its property.

This case does *not* present the question whether the rates which Allstate would be permitted to charge on the involuntary business are in fact adequate. As Allstate has always recognized, that depends on disputed facts and cannot be resolved on this record.

Contrary to the Appellate Division's ruling, however, this point does not end the inquiry. It only raises the question actually presented by Allstate: What procedures must New Jersey provide to protect against confiscation which may occur during the protracted rate proceedings? Cf. *First English Evang. Lutheran Church v. County of Los Angeles*, 482 U.S. 304 (1987) (right to just compensation for even temporary denial of use of property).

Questions of this sort recur regularly. They arise (1) in facial challenges to the validity of regulatory schemes;¹⁸ (2) in the form of requests to recoup rate deficits already incurred during the rate proceeding;¹⁹

¹⁸ See, e.g., *Guaranty Nat. Ins. Co. v. Gates*, 916 F.2d 508, 512-16 (9th Cir. 1990) (insurance statute facially invalid because it precluded timely rate adjustments); *Birkenfeld v. City of Berkeley*, 17 Cal. 3d 129, 165-74, 130 Cal. Rptr. 465, 491-97, 550 P.2d 1001, 1027-33 (1976) (same as to rent control ordinance); *Medical Malpractice Joint Underwriting Ass'n v. Paradis*, 756 F. Supp. 669, 675-77 (D.R.I. 1991) (specific provision of insurance statute precluding necessary adjustments invalid); *Calfarm v. Deukmejian*, 48 Cal. 3d 805, 258 Cal. Rptr. 161, 771 P.2d 1247 (1989) (same); *Helmsley v. Borough of Fort Lee*, 78 N.J. 200, 394 A.2d 65 (1978), *app. dismissed*, 440 U.S. 978 (1979) (same as to rent control ordinance).

¹⁹ See, e.g., *Hope Natural Gas v. FPC*, 196 F.2d 803, 808-09 (4th Cir. 1952) (retroactive application of rate increase to period

and (3) in the context of prospective requests to implement a provisional increase, subject to later refund if excessive, during the pendency of a rate proceeding. Some courts are receptive to interim rate requests²⁰ and others are not.²¹

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of rate proceedings impermissible); *Potomac Electric Power Co. v. Public Serv. Comm'n*, 380 A.2d 126 (D.C. 1977) (recoupment through future rate increase permissible for period between erroneous denial of rate increase and correction of that error); *New Rochelle Water Co. v. Pub. Serv. Comm'n*, 31 N.Y.2d 397, 340 N.Y.S.2d 617, 292 N.E.2d 767 (1972) (statute permitted recoupment through future rates of deficiencies during rate proceedings, but recoupment need not be provided where company had been assured at least some return, though less than a just return, during reasonably brief hearing); *Narragansett Elec. Co. v. Burke*, 119 R.I. 559, 381 A.2d 1358, 1364 (1977), *cert. denied*, 435 U.S. 972 (1978) (even though commission acted improperly in suspending rate increase for nine months, utility not entitled to recoup lost revenues).

²⁰ See, e.g., *Alaska Pub. Utilities Comm'n v. Greater Anchorage Area Borough*, 534 P.2d 549 (Alaska 1975) (interim rate increase required where disposition of rate proceeding not imminent, there was adequate showing of rate inadequacy, and ratepayers would be fully protected by refund mechanism); *Southern Bell Tel. & Tel. Co. v. Bevis*, 279 So. 2d 285 (Fla. 1973); *South Cent. Bell Tel. Co. v. Public Serv. Comm'n*, 555 So. 2d 1370 (La. App. 1990) (agency ordered decrease in rates); *Consumers Power Co. v. Michigan Public Service Comm'n*, 415 Mich. 134, 327 N.W.2d 875 (1982); *City of Tyler v. Television Cable Service, Inc.*, 481 S.W.2d 166 (Tex. Civ. App. Tyler 1972).

²¹ See, e.g., *Allstate Ins. Co. v. Gillespie*, 275 Cal. Rptr. 525 (Cal. App. 2d Dist. 1990), *depublished*, No. 5014332 (Cal. Feb. 21, 1991) (so long as rate proceeding conducted as expeditiously as possible, regulated company had no right to compel regulator to exercise power to grant interim rates because there is no right to be protected against interim losses during properly conducted proceeding); *Public Util. Comm'n v. Pedernales Elec. Co-op*, 678 S.W.2d 214 (Tex. App. Austin 1984), *writ ref'd n.r.e.* (no right to rate relief

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This Court had addressed such issues, most notably in *Prendergast v. New York Telephone Co.*, 262 U.S. 43 (1923), but has not done so for many years. Its guidance is required to resolve the confusion now afflicting other courts and to assure that adequate protection is provided to Allstate and other businesses threatened with interim confiscation. Review is also justified to address the implications of a regulatory system which allows New Jersey to draw on insurer income and assets generated in other states to subsidize New Jersey motorists.

A. New Jersey's Compulsion Of Allstate To Employ Its Property To Insure Depopulation Risks Requires That The State Provide A Mechanism Through Which Allstate Can Receive Just Compensation For The Insurance Provided.

This case involves an unusually aggravated form of the common problem just discussed. Allstate has not voluntarily undertaken to perform public service in return for a monopoly. To the contrary, scores of insurers provide automobile insurance in New Jersey. Nor has New Jersey simply prescribed the terms on which business may be done and left insurers the choice to proceed on those terms or not at all. Rather, New Jersey has compelled Allstate to do business on New Jersey's terms. Finally, Allstate has not *voluntarily* entered into commercial relationships which New Jersey requires it to *continue* (on altered terms) pursuant to newly enacted regulations. Instead, New Jersey demands that Allstate enter into

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during reasonable period of regulatory delay in processing rate application; also relying on statutory right to institute interim rate after application had been on file 90 days). The depublication of *Gillespie* means it is not precedential, even in California. But that case expressed candidly an approach which seems to underlie many less articulate (and often unreported) decisions by other tribunals.

*new involuntary relationships, on terms set entirely by the State.*²²

Allstate is a conscript, pure and simple. A State may conscript property, but the Constitution requires that it pay for the privilege.

New Jersey's conscription of Allstate to provide insurance to depopulation risks has far-reaching impacts on Allstate's nationwide business. The underwriting of insurance involves acceptance of premiums today in return for promises to pay losses in the future. Those promises must be backed with large financial assets if they are to be fulfilled. Since insurance claims require some time to be adjusted and paid, reserves must be maintained to cover losses which have already arisen but have not yet been paid.

If (1) losses were perfectly predictable, (2) rates were adequate, (3) reserves were properly determined, and (4) the insurer's assets were correctly valued and not subject to fluctuation, an insurer could theoretically operate with no assets other than its reserves and the facilities and equipment necessary for its operations. However, that would place the security of insureds at risk if any of those assumptions proved untrue. To minimize the likelihood that such contingencies might render the insurer unable to discharge its obligations to its insureds, the insurer must have substantial equity capital to serve as a "cushion" against such risks.²³

²² Compare *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419 (1982) (state authorization for utility to physically occupy portion of landlord's property to provide services to tenants constituted *per se* taking where landlord never agreed to such occupancy), with *FCC v. Florida Power Corp.*, 480 U.S. 245 (1987) (regulation altering contractually agreed price for use by tenant voluntarily accepted by owner did not constitute a taking in light of the fact that regulated price covered all owner's costs, including fully allocated cost of capital).

²³ See Kimball, *All Lines Authority: Implications for Solidity*, 11 Forum [now Tort & Insurance L.J.] 433, 437-38 (1976); H.

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To maintain assurance of solvency, insurance regulators and financial rating services prefer that insurers not write annual premium volumes exceeding roughly two to three times their equity capital. National Ass'n of Insurance Comm'rs, *Using the NAIC Insurance Regulatory Information System 7* (1990). Thus, regulatory constraints and customer concerns about an insurer's reliability limit, to a small multiple of its available capital, the total volume of insurance which it can write. In other words, forcing an insurer to write certain risks effectively forces it to allocate a portion of its capital to support those policies and makes that capital unavailable to support other policies.

How much capital must be allocated to a given group of policies while maintaining a given level of policyholder security depends on the level of risk of those policies, and the adequacy of the rates charged. If the risk is very unpredictable, more random fluctuations must be expected and more capital must be allocated. More importantly here, if the rates are inadequate (or their adequacy is doubtful), the capital required to back those policies must suffice both to absorb likely rate deficits and provide for normal fluctuations.

Thus, by forcing Allstate to write large numbers of risks at rates which are *prima facie* confiscatory, New Jersey has severely constrained Allstate's ability to use its capital to write insurance in other, more profitable markets, and has subjected Allstate's capital to the risks of the assigned policies. In effect, New Jersey has appropriated a portion of Allstate's capital to its own use. Moreover, the effect of New Jersey's actions is to allow it to apply income and assets generated by Allstate in other States to subsidize the cost of insurance for New Jersey motorists.

Where a State thus appropriates the use of private property, it must provide a mechanism to compensate the

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Denenberg & S. Kimball, eds., *Insurance Government and Social Policy: Studies in Insurance Regulation*, ch. 6 ("Capital and Surplus Requirements") (1969).

owner for the use of that property. *Williamson County Regional Planning Comm'n v. Hamilton Bank*, 473 U.S. 172, 194 (1985). Here, the only mechanism New Jersey has provided is the (prospectively set) rates which it permits for the mandated insurance. Hence, an insurer must be protected against rate inadequacy or it will have no assurance of just compensation.

B. Where A State Provides Compensation Exclusively Through Prospective Setting Of Rates For The Regulated Service, Protection Must Be Provided Against Confiscation During The Process Of Adjusting Those Rates.

Providing compensation through purely prospective rates is inherently risky to the regulated business. If the rate set is initially inadequate or becomes inadequate, and the rate adjustment process is lengthy, then the regulated business will suffer irrecoverable losses during that process. This risk is especially pronounced if the regulator may be motivated to manipulate the process so that rate proceedings take even more time, with no increase permitted until they are completed.²⁴

Unless losses suffered on account of currently inadequate rates will be compensated in the future, current confiscation cannot be permitted pending determination of a final rate. *Prendergast v. New York Telephone Co.*, 262 U.S. 43 (1923). In *Prendergast*, a telephone company was ordered to reduce its rates pending completion of hearings to set rates. The order was said to be "temporary," but (as is true in New Jersey) no procedure was

²⁴ In New Jersey's last gubernatorial election, automobile insurance rates were a major issue. One of Governor Florio's main campaign promises was to reduce those rates. Anthony DePalma, *Car Insurance: The Issue That Won't Go Away in New Jersey*, N.Y. Times, Nov. 4, 1989, sec. 1, p. 28, col. 1. Thus, it is in his political interest, and that of his appointee, the Commissioner, to suppress those rates in every way possible, regardless of the cost to insurance companies, which do not vote.

available to recoup any deficits which might be incurred while the "temporary" order was in effect. This Court sustained a preliminary injunction staying the rate reduction, but requiring the company to refund any charges above the level originally ordered which were later found excessive.

The Court held that the ostensibly temporary character of the order did not

deprive the Company of its right to relief at the hands of the court. The orders required the new reduced rates to be put into effect on a given date. They were final legislative acts as to the period during which they should remain in effect pending the final determination; and if the rates prescribed were confiscatory the Company would be deprived of a reasonable return upon its property during such period, without remedy, unless their enforcement should be enjoined. Upon a showing that such reduced rates were confiscatory the Company was entitled to have their enforcement enjoined pending the continuance and completion of the rate-making process.

Id. at 49. *Accord Smith v. Illinois Bell Tel. Co.*, 270 U.S. 587, 591-92 (1926); *Banton v. Belt Line Ry. Corp.*, 268 U.S. 413 (1925); *Oklahoma Nat. Gas Co. v. Russell*, 261 U.S. 290 (1923). *See also West Ohio Gas Co. v. PUC*, 294 U.S. 79, 83 (1935) ("Present confiscation is not atoned for by merely holding out the hope of a better life to come").

C. The Procedures Utilized By A State To Protect Against Confiscation Must Include Independent Judicial Review Of The Need For Current Relief.

New Jersey has taken the view that the propriety of rates whose regulation is entrusted to an administrative agency may not be considered by a court in the first instance. *In Re Industrial Sand Rates*, 66 N.J. 12, 19, 327 A.2d 427, 431 (1974). The agency must, as a precondition to judicial review, first marshal and sift the relevant facts, providing the benefit of its expert analysis. *Id.* The Constitution permits such a

limitation. *St. Joseph Stock Yards Co. v. United States*, 298 U.S. 38, 52-53 (1936). The reviewing court may give considerable weight to the administrative findings. *Id.*

But the supremacy of the Constitution over state law does not permit a state legislature to remit the question of confiscation solely to the unbridled discretion of an administrative officer. This Court so held in *St. Joseph Stock Yards*, first noting that (*id.* at 51-52):

the Constitution fixes limits to the rate-making power by prohibiting the deprivation of property without due process of law or the taking of private property for public use without just compensation. When the Legislature acts directly, its action is subject to judicial scrutiny and determination in order to prevent the transgression of these limits of power. The Legislature cannot preclude that scrutiny or determination by any declaration or legislative finding. Legislative declaration or finding is necessarily subject to independent judicial review upon the facts and the law by courts of competent jurisdiction to the end that the Constitution as the supreme law of the land may be maintained.

This principle applies equally where a legislature has entrusted the ratemaking power to an administrative agency:

Nor can the Legislature escape the constitutional limitation by authorizing its agent to make findings that the agent has kept within that limitation. Legislative agencies, with varying qualifications, work in a field peculiarly exposed to political demands. Some may be expert and impartial, others subservient. It is not difficult for them to observe the requirements of law in giving a hearing and receiving evidence. But to say that their findings of fact may be made conclusive where constitutional rights of liberty and property are involved, although the evidence clearly establishes that the findings are wrong and constitutional rights have been invaded, is to place those rights at the mercy of administrative officials and seriously

to impair the security inherent in our judicial safeguards.

Id. at 52.

Judicial review is particularly necessary where, as here, the administrative agency is institutionally biased, since it must impose costs either on the party claiming confiscation or on the mass of ratepayers to which the agency is politically responsible. Moreover, the Supremacy Clause itself relies on state courts as a primary means of assuring that state government is kept within constitutional limits. U.S. Const., art. VI, cl. 2 ("The Constitution . . . shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby. . . ."). To allow a state legislature to preclude judicial review of questions of confiscation would allow it to evade constitutional commands.

Thus, if a State chooses, as New Jersey has, to limit initial determination of questions of rate adequacy to administrative officers, then it must protect private parties asserting substantial claims of confiscation during the pendency of protracted administrative proceedings. When such an officer is faced with a *prima facie* showing that his contemplated action will have a confiscatory effect, the officer must either protect the party claiming confiscation (by such devices as deferral of the challenged action or interim rate relief) or determine, on a record susceptible to judicial review, that no protection is necessary.²⁵ Cf. *Jersey Central Power & Light Co. v. Federal Energy Regulatory Comm'n*, 810 F.2d 1168, 1177-79 (D.C. Cir. 1987) (en banc) (Bork, J.) (where agency applies policy which is ordinarily valid but which regulated party claims will have a confiscatory impact in the particular situation, agency must conduct evidentiary proceedings to evaluate the claim of confiscation). New Jersey has denied Allstate the requisite level of procedural protection.

²⁵ It is unnecessary in this case to determine what standard should be applied by the administrative officer and the reviewing court. One possibility would be the familiar standard applied to preliminary injunction motions, as interim rates are essentially a form of administrative preliminary relief.

D. Allstate Has Made A Sufficient Showing To Require Further Proceedings Before It May Be Subjected To The Risk Of Confiscation.

The declarations filed by Allstate's actuaries (Aa 43A-44A) make out a prima facie case of confiscation. They are strongly supported by the independent actuarial reports (Aa 187A-227A; Aa 140A-144A; App. 13), *most of which were prepared by the Commissioner's own consultants*. But the most compelling prima facie support for finding confiscation here flows from the operation of New Jersey's regulatory system itself.

Once rates have been fixed which are just and reasonable, they are presumed to remain just and reasonable until the contrary is shown. *See, e.g., Swift & Co. v. United States*, 343 U.S. 373, 382-83 (1952). Where, as with the JUA/MTF, rates were deliberately set at a level which was not just and reasonable, even with the subsidies formerly provided by RMEC's and policy constants, then it should likewise be presumed that they have not spontaneously become just and reasonable.

Nor can this presumed inadequacy on the assigned business be made up by any excess profit on Allstate's other New Jersey business. Allstate's present automobile insurance rates were approved by the Commissioner long before FAIRA.²⁶ Even if, despite FAIRA's imposition of

²⁶ Allstate's last general rate increase took effect in March, 1989. Since that time, Allstate has taken three flex-rate increases, which are designed solely to protect Allstate against inflationary cost increases. *N.J. Stat. Ann.* 17:29A-44a. Such increases are based on the percentage increase of specified components of the Consumer Price Index, relating to medical services and automobile repairs. The losses incurred by insureds (which Allstate promises to pay) reflect those cost increases, so that flex-rate increases simply maintain the pre-existing level of rate adequacy or inadequacy unchanged by

new taxes and assessments, Allstate's voluntary-market rates could be presumed to remain adequate for voluntary business, they surely must also be presumed not to be excessive for that business. Accordingly, the voluntary business can provide no excess profits to subsidize losses from the depopulation assignments.

In short, the New Jersey system of rate regulation itself supports a presumption that the Depopulation Order *will* have a confiscatory effect on Allstate.

CONCLUSION

For all the foregoing reasons, a writ of certiorari should issue to review the decision of the Appellate Division.

Respectfully submitted,

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(Continued from previous page)

the effects of those cost factors. Such increases cannot themselves correct for pre-existing rate inadequacy or render adequate rates excessive. Nor can they correct for any rate inadequacy or excessiveness created by circumstances, other than price increases, such as changes in the law.

Allstate has also been permitted to implement a non-standard risk rating plan (effective January 1, 1992), which will slightly increase (by about 3%) its voluntary-market revenue levels. (Aa 289A, ¶ 11) Such an increase cannot possibly overcome the overwhelmingly larger effects of such costs imposed by FAIRA as the new taxes and assessments (totalling 7.7% of premium). Thus, the non-standard risk rating plan could not produce any excess profits in the voluntary market to subsidize depopulation losses.



DEC 17 1991

OFFICE OF THE CLERK

In The

Supreme Court of the United States

October Term, 1991

ALLSTATE INSURANCE COMPANY,
an Illinois Corporation,

Petitioner,

v.

SAMUEL F. FORTUNATO,
Commissioner of Insurance of
The State of New Jersey,

Respondent.

Petition For A Writ Of Certiorari To The
Appellate Division Of The Superior
Court Of The State Of New Jersey

APPENDIX, VOLUME I

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APPENDIX 1

ORDER NO. A 91-111

STATE OF NEW JERSEY
DEPARTMENT OF INSURANCE

IN THE MATTER OF THE)
ASSIGNMENT OF EXPOSURES TO)
Allstate Insurance Company, A) ORDER
MEMBER COMPANY OF THE)
NEW JERSEY AUTOMOBILE FULL)
INSURANCE UNDERWRITING)
ASSOCIATION AND THE)
MARKET TRANSITION FACILITY)
OF NEW JERSEY, PURSUANT TO)
THE VOLUNTARY MARKET)
PLACEMENT PROGRAM)

This matter having been opened by the Commissioner of Insurance of the State of New Jersey ("Commissioner") pursuant to the authority of N.J.S.A. 17:1C-1 *et seq.*, N.J.S.A. 17:30E-1 *et. seq.*, the Fair Automobile Insurance Reform Act of 1990 ("FAIR Act") (P.L. 1990, c. 8) (N.J.S.A. 17:33B-1 *et seq.*), and all powers expressed or implied therein; and

IT APPEARING that N.J.S.A. 17:30E-14(a), as amended by P.L. 1988, c. 119, requires the Commissioner to establish procedures in the Plan of Operation ("Plan") of the New Jersey Automobile Full Insurance Underwriting Association ("Association") to govern the voluntary writings of applicants and Association insureds without utilization of the Association; and

IT FURTHER APPEARING that the enactment of the FAIR Act further amends N.J.S.A. 17:30E-14 and requires

the Commissioner to make additional amendments to the Association's Plan; and

IT FURTHER APPEARING that the Commissioner certified amendments to the Association's Plan, entitled the Voluntary Market Placement Program ("Program") (Operating Principles, Part I, Section 13), on April 28, 1989 and on November 14, 1990 and proposed additional amendments to the Program on December 31, 1990; and

IT FURTHER APPEARING that N.J.S.A. 17:30E-14 (c), as amended by P.L. 1988, c. 119, and the procedures set forth in the Program, require the Commissioner to direct the Association to assign to member companies the balance of exposures needed to meet the applicable quota in the event that any quota established by the Commissioner was not met by the end of the applicable quota period; and

IT FURTHER APPEARING that the member companies were notified by letter dated May 15, 1990 of their apportionment share for the depopulation quota period ending September 30, 1990; and

IT FURTHER APPEARING that the depopulation quota established by the Commissioner for the period ending September 30, 1990 was not met according to the quarterly reports filed by the member companies with the Department of Insurance listing in force exposures by territory as of September 30, 1990; and

IT FURTHER APPEARING that Allstate Insurance Company ("Allstate") failed to meet its assigned apportionment share by 32,687 exposures as of September 30, 1990; and

IT FURTHER APPEARING that, pursuant to *N.J.S.A. 17:33B-1 et seq.*, and amendments to *N.J.S.A. 17:30E-1 et seq.*, the Association has been succeeded in function and responsibility by the Market Transition Facility of New Jersey ("MTF").

THEREFORE, IT IS on this 24th day of January, 1991,

ORDERED that mandatory assignment of exposures from Association or MTF policies expiring on or after April 1, 1991 be effective upon approval by the Board of Directors of the Association of the amendments to the Association's Voluntary Market Placement Program proposed on December 31, 1990 or upon certification of these proposed amendments on January 31, 1991 pursuant to *N.J.S.A. 17:30E-6*, whichever occurs first; and

IT IS FURTHER ORDERED that the Association and MTF assign 32,687 exposures to Allstate in accordance with the provisions of the Mandatory Depopulation Assignment Plan attached hereto as Exhibit 1; and

IT IS FURTHER ORDERED that Allstate shall comply with the provisions of the Mandatory Depopulation Assignment Plan; and

IT IS FURTHER ORDERED that Allstate shall make offers of automobile insurance coverage and/or issue automobile insurance policies to every Association or MTF policyholder assigned to it pursuant to the Mandatory Depopulation Assignment Plan; and

IT IS FURTHER ORDERED that Allstate shall offer the same or equivalent automobile insurance coverage to every assigned Association or MTF policyholder where Allstate has rates and rules for such coverage filed and

approved by the Department. Where Allstate does not have rates and rules filed and approved by the Department for the same or equivalent coverage presently afforded the assigned policyholder under the Association or MTF policy, Allstate shall offer to the assigned Association or MTF policyholder the next broadest coverage for which Allstate has rates and rules filed and approved by the Department. Provided, however, that in no event shall Allstate offer less coverage to the assigned Association or MTF policyholder than the coverage afforded to the assigned policyholder under the Association or MTF automobile insurance policy; and

IT IS FURTHER ORDERED that Allstate shall, upon acceptance of the automobile insurance coverage by the Association or MTF policyholder, write and service the assigned exposure(s) for a minimum period of one (1) year from the expiration date of the assigned Association or MTF policy. Except for nonpayment of premium, Allstate shall not be permitted to decline coverage or cancel, nonrenew or otherwise terminate any assigned exposure during this one (1) year period; and

IT IS FURTHER ORDERED that Allstate shall be precluded from requiring the assigned Association or MTF policyholder to obtain or maintain membership or qualification for membership in any club, group or organization as a condition for providing automobile insurance coverage, including the payment of dues, membership fees, or other charges;

IT IS FURTHER ORDERED that Allstate shall be fined \$2,000.00 for every offer of automobile insurance coverage or policy of automobile insurance which Allstate fails to make or issue at least thirty (30) days prior

to the expiration date of the assigned Association or MTF policy. Pursuant to *N.J.S.A. 17:30E-17(a)*, all fines shall be collected and enforced in accordance with *N.J.S.A. 2A:58-1 et seq.* (the "Penalty Enforcement Law"); and

IT IS FURTHER ORDERED that Allstate shall be subject to any other penalty provision of *N.J.S.A. 17:30E-17*, and any other penalties authorized by law, if Allstate fails to comply with the terms of this Order and the provisions of the Mandatory Depopulation Assignment Plan.

<hr style="width: 20%; margin: 0 auto;"/> Date	/s/ <u>Samuel F. Fortunato</u> Samuel F. Fortunato Commissioner
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EXHIBIT 1

MANDATORY DEPOPULATION ASSIGNMENT PLAN

The following procedures shall govern the assignment of exposures by the New Jersey Automobile Full Insurance Underwriting Association ("Association") and the Market Transition Facility of New Jersey ("MTF") to every member company which failed to write its apportionment share established by the Commissioner of Insurance of the State of New Jersey ("Commissioner") for the depopulation quota period which ended September 30, 1990:

1. Assignment of private passenger automobile non-fleet exposures ("exposures") shall be made from those rating territories where the voluntary market share is less than the aggregate voluntary market quota established by the Commissioner. Pursuant to *N.J.S.A. 17:30 E-14(b)(2)* and the aggregate voluntary market quota

established by the Commissioner, the member companies were to have voluntarily written 68 percent of the exposures in the total private passenger automobile insurance market in New Jersey by September 30, 1990. Accordingly, based on the quarterly reports filed by the member companies with the New Jersey Department of Insurance ("Department") listing in force exposures as of September 30, 1990, any rating territory where the voluntary market share is less than 68 percent of the total market (for that territory) shall be included in the Mandatory Depopulation Assignment Plan as a territory subject to assignments.

2. The quarterly reports filed by member companies listing in force exposures as of September 30, 1990 indicated that those member companies that failed to write their apportionment shares, in the aggregate, fell short by 222,977 exposures. The assignment of exposures to these member companies shall be made from the territories subject to assignments in the percentages indicated below. The assignment percentages were determined by:

a. assigning a sufficient number of exposures from the rating territory which had the smallest voluntary market share until the voluntary market share of this rating territory equaled the voluntary market share of the rating territory which had the next smallest voluntary market share; then

b. assigning a sufficient number of exposures from these two rating territories until their voluntary market share equaled the voluntary market share of the rating territory which had the third smallest voluntary market share; then

c. repeating step (b) above with additional rating territories until 222,977 exposures were assigned from the territories subject to assignments. Provided, however, that the adjusted voluntary market share of any territory subject to assignments shall not exceed 68 percent.

<u>Rating Territory No.</u>	<u>Brief Territory Description</u>	<u>Assignment Percentages</u>
01	Jersey City	19.37%
03	Paterson	14.28%
02	Newark	12.62%
04	Elizabeth	12.09%
22	Newark Semi-Suburban	06.21%
38	E. Orange/Orange	05.51%
11	S. Bergen County	05.12%
07	Camden	04.27%
08	Perth Amboy	03.48%
27	Atlantic County	03.29%
23	Hudson County	03.03%
40	New Brunswick	02.60%
13	Camden County	
	(Balance)	02.48%
05	Bayonne	01.68%
14	Gloucester County	01.58%
19	Atlantic City	01.01%
16	Long Branch	00.81%
06	Trenton	00.57%

3. The number of exposures assigned to each member company shall be increased by an acceptance factor of 25 percent. It is the expectation of the Department that not every offer of coverage made by a member company to its assigned policyholders will be accepted. This expectation is based on the dynamic aspect of the New Jersey automobile insurance market (i.e. Association or MTF policyholders independently seeking coverage with a

voluntary insurer, competition among member companies to write additional new business in order to meet future depopulation quotas, and Association or MTF policyholders leaving New Jersey).

For the purposes of the Mandatory Depopulation Assignment Plan, offer of coverage means making an offer of automobile insurance coverage at least 30 days prior to the expiration date of the assigned Association or MTF automobile insurance policy (for those member companies that make offers of coverage to applicants prior to the issuance of the automobile insurance policy) or issuing a policy of automobile insurance at least 30 days prior to the expiration date of the assigned Association or MTF automobile insurance policy (for those member companies that do not make offers of coverage to applicants).

4. Exposures shall be assigned to member companies from the book(s) of business of Association or MTF producers who shall be randomly selected from territories subject to assignments based on the size of the producer's book of business and the shortfall of the member company. Selection of producers shall be made by the Department in accordance with item 18 below. For purposes of the Mandatory Depopulation Assignment Plan, every exposure insured by the Association or MTF is eligible for assignment.

5. For purposes of this Mandatory Depopulation Assignment Plan, it shall be deemed that the assigned exposures are located in the rating territory of the principal business address of the selected producer, regardless of the rating territory where the exposures actually are located.

6. a. The member company shall make offers of coverage to every assigned Association or MTF policyholder at least 30 days prior to the expiration date of the assigned Association or MTF policy (i.e. upon renewal of the Association or MTF policy). The offer of coverage shall include, for each assigned exposure, the coverages, limits, options and deductibles transferred to the member company under item 19 below.

b. The member company shall include with the offer of coverage the statements of privacy practices required by law (e.g. Insurance Information Practices Act (N.J.S.A. 17:23A-1 *et seq.*); Fair Credit Reporting Act). The member company may include an authorization form to be signed by the assigned Association or MTF policyholder in order to obtain investigative consumer reports. Provided, however, that the failure of the assigned policyholder to return a signed authorization form shall not be grounds for the member company to decline coverage, or cancel, nonrenew or otherwise terminate the policy during the one (1) year period.

c. The member company shall mail a copy of the offer of coverage to the producer of the mandatorily assigned exposures. The copy of the offer of coverage which the member company would provide its own agent if the business had been written voluntarily is sufficient for purposes of this paragraph (see item 16 below).

7. The member company is expressly prohibited from requiring the assigned Association or MTF policyholder to obtain or maintain membership or qualification for membership as a condition for providing

automobile insurance coverage, including, but not limited to, charging dues, membership fees or other charges.

8. The member company must continue to make offers of coverage to all assigned Association or MTF policyholders even when the member company has written sufficient exposures to meet its apportionment share shortfall. Any exposures written in excess of the apportionment share shortfall may be used by the member company toward the fulfillment of its next apportionment share.

9. a. The member company shall include the applicable policyholder assignment notice attached hereto as Exhibits 2 and 3 with every offer of coverage mailed to the assigned Association or MTF policyholder. Exhibit 2 shall be included with offers of coverage for Association policies expiring before October 1, 1991. Exhibit 3 shall be included with offers of coverage for MTF policies expiring on or after October 1, 1991.

b. Except for format changes, any change to the policyholder notice must be approved by the automobile Residual Market Unit of the Department before such notice is mailed to any Association or MTF policyholder (e.g. changes to the required information, adding additional information to the notice, changes in type point-size). For purposes of this paragraph, format change means only the realignment of the required information to accommodate the various data processing systems of the member companies.

c. The type size used in the policyholder notices shall be at least 10-point. The type style used in the policyholder notices shall be the same type style used by

the member company in the Buyer's Guide (N.J.A.C. 11:3-15.1 *et seq.*). The size of the paper shall be eight and one-half inches by eleven inches. The member company may print the required notice on both sides of the paper.

10. It is the responsibility of the member company to be able, upon request, to demonstrate to the satisfaction of the Department, Association or MTF that an offer of coverage, including the policyholder assignment notice, was mailed to the assigned Association or MTF policyholder.

11. The member company shall offer the same or equivalent automobile insurance coverage, which was afforded under the Association or MTF policy, to every assigned Association or MTF policyholder where the member company has rates and rules for such coverage filed and approved by the Department. Where the member company does not have rates and rules filed and approved by the Department for the same or equivalent coverage presently afforded the assigned policyholder under the Association or MTF policy, the member company shall offer to the assigned Association or MTF policyholder the next broadest coverage for which the member company has rates and rules filed and approved by the Department. The member company is expressly prohibited from offering less coverage to the assigned policyholder than the coverage afforded to such policyholder under the Association or MTF policy.

The following examples are provided for illustration purposes only:

Example 1: The Association or MTF policyholder presently has \$25,000/\$50,000/\$10,000 split

limits of liability coverage. However, the member company that has been assigned this policyholder only writes combined single limit of liability coverage and only has rules and rates filed and approved by the Department for this type coverage. Therefore, the member company must offer the Association or MTF policyholder a combined single limit of liability coverage which is equal to the bodily injury occurrence limit and the property damage occurrence limit added together or the next broadest available coverage (e.g. \$75,000, but in no event less than \$60,000).

Example 2: The Association or MTF policyholder presently has \$25,000/\$50,000/\$10,000 split limits of liability coverage. The member company that has been assigned this policyholder only writes combined single limit of liability coverage and offers \$100,000 combined single limit of liability coverage as the minimum coverage to its voluntary insureds. However, the member company has rates and rules filed and approved by the Department for combined single limit of liability coverage for amounts less than \$100,000. Therefore, the member company must offer the Association or MTF policyholder a combined single limit of liability coverage which is equal to the bodily injury occurrence limit and the property damage occurrence limit added together or the next broadest available coverage, but less than \$100,000 (e.g. \$75,000, but in no event less than \$60,000).

Example 3: The Association or MTF policyholder presently has \$25,000/\$50,000/\$10,000 split limits of liability coverage. The member company that has been assigned this policyholder only writes combined single limit of liability coverage and offers \$100,000 combined single limit of liability coverage as the minimum

coverage to its voluntary insureds. The member company does not have any rates and rules filed and approved by the Department for amounts of combined single limit of liability coverage less than \$100,000. Therefore, the member company must offer the Association or MTF policyholder \$100,000 combined single limit of liability coverage.

Example 4: The Association or MTF policyholder presently has \$75,000 combined single limits of liability coverage. The member company that has been assigned this policyholder writes both split limits and combined single limit of liability coverage and has rates and rules filed and approved by the Department for both types of coverage. Therefore, the member company must offer the Association or MTF policyholder \$75,000 combined single limit of liability coverage and not a split limits policy.

Example 5: The Association or MTF policyholder presently has \$100,000 combined single limit of liability coverage. The member company that has been assigned this policyholder writes only split limits of liability coverage and only has rates and rules filed and approved by the Department for this type of coverage. Therefore, the member company must offer the Association or MTF policyholder split limits of liability coverage with a bodily injury per person limit equal to the combined single limit of liability coverage or the next broadest available coverage (e.g. \$100,000/\$300,000/\$50,000). (Note: All conversions of combined single limit of liability coverage should be handled in the same manner, except a \$35,000 combined single limits policy. In this

particular case, the member company shall offer \$15,000/\$30,000/\$5,000 split limits of liability coverage.)

12. a. Upon acceptance of the offer of coverage by the Association or MTF policyholder, the member company shall, at a minimum, write and service the assigned exposure(s) for a period of one (1) year from the policy expiration date of the assigned Association or MTF policy, regardless of the member company's customary policy term (e.g. 6 months).

b. For purposes of this paragraph, writing and servicing the assigned exposure shall be given the broadest possible meaning while the policy is in force, including, but not limited to, adjusting claims resulting from accidents, adding or deleting vehicles, adding or deleting drivers and adding, changing or deleting coverages, limits, options or deductibles. The member company shall provide any change properly requested by the assigned policyholder during the mandatory one (1) year assignment period for which the member company has rates and rules filed and approved by the Department. Essentially, the assigned Association or MTF policyholder shall have the same rights during this one (1) year period as if the policy were insured through the Association or MTF.

13. Upon acceptance of the offer of coverage, the member company shall be permitted to charge additional premium in accordance with its rates and rules filed and approved by the Department based on subsequent information supplied to the member company (e.g. undisclosed motor vehicle violations and/or accidents, new

motor vehicle or change in coverage requested by policyholder).

14. a. Included with the offer of coverage or upon acceptance of the offer of coverage by the assigned Association or MTF policyholder, the member company shall provide the assigned Association or MTF policyholder with a Coverage Selection Form and the New Jersey Auto Insurance Buyer's Guide ("Buyer's Guide"). The coverage Selection Form shall be filled in by the member company with the applicable information provided to the member company by Equifax Services, Inc. ("Equifax") in accordance with item 19 below (e.g. policyholder name, coverages, limits, options and deductibles). The member company shall ask the assigned Association or MTF policyholder to sign and return the Coverage Selection Form. The assigned policyholder has the right to elect different coverages, limits, options and deductibles.

b. Where the assigned Association or MTF policyholder has accepted coverage with the member company but has failed to return a signed Coverage Selection Form, the member company shall send a second completed Coverage Selection Form and Buyer's Guide to the assigned policyholder in accordance with the proof of mailing procedures set forth in *N.J.S.A. 17:29C-10*. The second Coverage Selection Form and Buyer's Guide shall be accompanied by the applicable policyholder notice attached hereto as Exhibits 4 and 5. Exhibit 4 shall be utilized for Association policies expiring before October 1, 1991, while Exhibit 5 shall be utilized for MTF policies expiring on or after October 1, 1991. These notices shall inform the policyholder that failure to return a signed Coverage Selection Form to the member company will

result in the tort option and the physical damage deductibles being changed to the statutory defaults (i.e. lawsuit threshold, \$500 physical damage deductibles). The policyholder notices shall follow the same requirements set forth under item 9 above (i.e. type size, type style, changes to the notice, paper size). Provided, however, that the failure of the assigned policyholder to return a signed Coverage Selection Form shall not be grounds for the member company to cancel or otherwise terminate the policy.

15. The member company shall comply with all applicable New Jersey statutes and regulations in providing coverage to the assigned Association or MTF policyholder (e.g. mandatory physical damage inspection).

16. In providing coverage to the assigned Association or MTF policyholder, the member company shall issue the policy in accordance with its voluntary business practices to the extent practicable. Provided, however, that the member company shall not be permitted to utilize its voluntary business practices during this one (1) year period where such practices are more restrictive than the standards utilized by the Association or MTF.

For example, the Association and MTF presently permit the policyholder to pay the annual premium in four (4) installment payments. The last payment is due 180 days after the effective date of the policy. A member company cannot use its voluntary installment payment plan if such plan requires the assigned policyholder to pay the annual premium in less than four (4) installments or less than 180 days from the effective date of the policy.

17. Except for nonpayment of premium, the member company shall not be permitted to decline coverage or cancel, nonrenew or otherwise terminate the assigned exposure during this one (1) year period. Upon expiration of this one (1) year period, the member company may cancel or nonrenew the assigned exposure in accordance with New Jersey statutes and regulations in effect at the time of cancellation or nonrenewal.

18. a. Where a member company that is subject to the Mandatory Depopulation Assignment Plan has an existing voluntary relationship with a producer of the Association or MTF who is located in one of the territories subject to assignments identified in item 2 above, the producer's entire Association and/or MTF book of business may be assigned to such member company to the extent necessary to meet the member company's mandatory assignments.

1. Where a producer has a voluntary relationship with two (2) or more member companies that are subject to the Mandatory Depopulation Assignment Plan, the producer shall be deemed to be the producer of the member company having the largest mandatory assignment amount.

b. Where a member company's mandatory assignments for a territory subject to assignment cannot be satisfied from the book(s) of business from producer(s) selected pursuant to paragraph (a) above, the member company shall be assigned the entire Association and/or MTF book of business from producers who do not have

an existing voluntary relationship with any member company and who are located in one of the territories subject to assignments.

c. For purposes of the Mandatory Depopulation Assignment Plan, producers shall be selected from two (2) random lists by territories subject to assignments created by the Department from the results of the Producer Survey dated July 16, 1990. The first list, which shall be used to select producers pursuant to paragraph (a) above, shall contain those producers who have a voluntary market relationship with a member company. The second list, which shall be used to select producers pursuant to paragraph (b) above, shall contain those producers who do not have a voluntary relationship with any member company.

19. Each month for twelve (12) consecutive months after the effective start date of the Mandatory Depopulation Assignment Plan, each member company that is subject to mandatory assignment of exposures shall receive policy information from Equifax approximately 35-40 days prior to the expiration date of the assigned Association or MTF policy. To the extent practicable, each member company shall receive their monthly mandatory assignments by computer tape (cartridge, reel or any media mutually agreed to by Equifax and the member company). Unless the member company and Equifax mutually agree to a different record format, Equifax shall provide the policy information to the member company in the record format set forth in the Exhibit 6 (similar to the record format set forth in the Association's Plan of Operation, Operating Principles, Part II - Servicing Carriers, Exhibit M). Member companies may elect to receive

their mandatory assignments from Equifax by paper printout. Member companies may contract separately with Equifax to have Equifax provide additional information concerning the mandatorily assigned exposures and/or receive the policy information in a different record format than that set forth in Exhibit 6.

For purposes of illustration only, the Mandatory Depopulation Assignment Plan requires member companies to begin offering coverage to assigned exposures no later than March 1, 1991 for Association or MTF policies due to expire on April 1, 1991. Between March 15 and March 20, 1991, Equifax will endeavor to send to the member company either a computer tape or paper printout listing all the assigned Association or MTF policies due to expire during the month of April, 1991.

20. a. All member companies shall be permitted to use MTF rates and rules as authorized by N.J.S.A. 17:33B-11(c)(2) and N.J.S.A. 17:33B-12 for the exposures mandatorily assigned from the Association or MTF. Where a member company chooses to use MTF rates and rules, the member company shall pay the producers of the mandatorily assigned exposures the same commission paid by the MTF to its producers (MTF presently pays its producers a nine percent annual commission). The applicable MTF rule and rate pages shall be made available to member companies.

b. Where a member company chooses to use its own rates and has a voluntary relationship with the producer of the mandatorily assigned exposures, the member company shall pay the producer the same

renewal commission it would have paid such producer if such exposures had been renewed voluntarily.

c. Where a member company chooses to use its own rates and does not have an [sic] voluntary relationship with the producer of the mandatorily assigned exposures, the member company shall negotiate in good faith with each producer, or all the producers as a group, to determine the commission to be paid to such producer(s) for the mandatorily assigned exposures. Provided, however, that the commission agreed to between the member company and such producer shall be equivalent to the compensation paid to, or on behalf of, its own agents for renewal business (e.g. advertising expenses, office overhead expenses, contingent commissions). For purposes of this provision, agent shall be construed to have the broadest possible meaning, including, but not limited to, exclusive agents or independent agents.

d. In the case of member companies that are direct writers, while their rates do not include specific expenses for commissions paid to agents, their rates do include expenses for a direct marketing department and related support staff. This expense must be considered in determining the commission to be paid to producers under paragraph (c) above. Provided, however, that the commission agreed to by the direct writer and the producer under paragraph (c) above shall be equivalent to the compensation paid to independent agents for renewal business by member companies that utilize such agents.

e. All member companies shall pay commissions to producers of the mandatorily assigned exposures

so long as the member company continues to insure such exposures.

21. The member company shall be permitted to use prospectively rates and rules filed and approved by the Department after the start of the Mandatory Depopulation Assignment Plan. Provided, however, member companies that issue six (6) month policies shall be precluded from using the new rates and rules in issuing the second six (6) month policy, but rather shall use the same rates and rules which were used in issuing the first six (6) month policy.

22. The producer of the mandatorily assigned exposures has no right to place new business with the member company, unless the producer and member company enter into a voluntary relationship. Provided, however, that the producer of the mandatorily assigned exposures has the right to submit endorsement change request forms on behalf of the assigned policyholder if requested to do so by the policyholder. Any such change in coverage, limits, options or deductibles submitted by the producer on behalf of the policyholder shall be effective immediately and not upon subsequent approval of the member company.

23. For purposes of the Mandatory Depopulation Assignment Plan, the performance standards governing the conduct of producers of the mandatorily assigned exposures shall be the applicable MTF Producer Standards (MTF Plan of Operation, Operating Principles, Part III - Producers). Essentially, the member company is prohibited from requiring the producer of the mandatorily assigned exposures to satisfy greater requirements than

those required by the MTF (e.g. member company cannot compel producer to obtain Errors and Omissions coverage). These standards shall apply until October 1, 1992. After this date, the member company shall apply its own producer performance standards.

24. The member company shall report to the MTF cases of producer misconduct where the member company believes that the producer of the mandatorily assigned exposures is not complying with the applicable MTF performance standards. In reporting such cases, the member company shall provide detailed documentation to the MTF which evidences such producer misconduct. The member company shall provide such other information as may be requested by the MTF. The MTF shall consider such charges and shall take appropriate disciplinary action, including, but not limited to, revocation or termination of the producer's MTF contract. Provided, however, that no failure on the part of the producer of the mandatorily assigned exposures to properly perform under the provisions of the MTF Producer Standards shall prejudice the rights of a good faith assigned policyholder to coverage with the member company.

25. The MTF shall notify the member company of those cases where the MTF contract of the producer of the mandatorily assigned exposures is revoked or terminated by the MTF or where it subsequently determined by the MTF that the producer of the mandatorily assigned exposures does not have a [sic] MTF producer contract. Upon such notification from the MTF, the member company shall be under no obligation to pay any commission to such producer of the mandatorily assigned exposures and

may reassign such exposures to its own agents for servicing.

26. The member company shall recognize a producer of record change for the mandatorily assigned exposures and shall follow its normal voluntary business practices (e.g. cancellation of the old policy and rewrite of the new policy). Provided, however, that the member company shall rewrite the policy for at least the one (1) year period from which the exposure was originally assigned to the member company.

27. Each month for fourteen (14) consecutive months after the effective start date of the Mandatory Depopulation Assignment Plan, each member company shall report separately the following information to the Department concerning the exposures assigned to it:

a. The number of policy records received from the Equifax;

b. The number of offers of coverage issued for the assigned exposures;

c. The number of offers of coverage accepted by the assigned Association or MTF policyholders and the number of exposures in force by territory; and

d. The number of policies which are canceled or nonrenewed. Whenever a policy is canceled or nonrenewed, the member company shall provide the Department with a separate report from that required by this provision indicating the policyholder's name, address (including zip code), telephone number (including area code), policy number and the specific reason why such policy was canceled or nonrenewed.

28. The information required by item 27 above shall be delivered and received by the Department no later than the close of business on the 20th calendar day of the month such report is due. Where the 20th calendar day falls on a weekend or holiday, the report is due by the close of the next business day. The report and the content of the report required by item 27 above shall be prescribed by the Department and is attached hereto as Exhibit 7. The report required by item 27 above shall be mailed to the Department at the following address:

New Jersey Department of Insurance
Automobile Residual Market Unit
20 West State Street
CN 329
Trenton, New Jersey 08625-0329

If the Mandatory Depopulation Assignment Plan requires member companies to begin offering coverage to assigned exposures no later than March 1, 1991 for Association and MTF policies due to expire on April 1, 1991, the first member company report would be due April 20, 1991 and each month thereafter until the last report is submitted on June 20, 1992.

29. All costs associated with the administration of this Mandatory Depopulation Assignment Plan, as approved by the Commissioner, shall be paid by the member companies that are subject to mandatory assignments. Such costs shall include, but are not limited to, computer time of the Equifax, Association and/or MTF servicing carriers; programming costs; cost of computer tapes; reproduction of MTF rate pages; postage and priority mail service.

30. The Commissioner reserves the right to make additional assignments pursuant to the Mandatory Depopulation Assignment Plan if he determines that the goals of such plan are not being met based on the reports filed by the member companies pursuant to item 27 above.

31. The Commissioner reserves the right to revise the provisions of the Mandatory Depopulation Assignment Plan as he deems necessary in order to accomplish the goals of such plan.

EXHIBIT 2

(MEMBER COMPANY LETTERHEAD
INFORMATION GOES HERE)

(Insert mailing date of notice)

Newly Assigned Automobile Insurance Company:

(Insert member company name)

(Insert member company address, including city, state & zip code)

(Insert 800 toll free policyholder telephone number, if available or New Jersey telephone number, including area code, where policyholder can call for general information)

Previous Automobile Insurance Company:

New Jersey Automobile Full Insurance Underwriting Association (JUA)

Serviced by: (Insert name of JUA servicing carrier)
JUA Policy Number: (Insert JUA policy number)

JUA Policy Expiration Date: (Insert policy expiration date)

Policyholder:

(Insert name of policyholder)

(Insert policyholder's address, including city, state & zip code)

Dear Policyholder:

Your automobile insurance policy with the New Jersey Automobile Full Insurance Underwriting Association (JUA) expires on (insert JUA policy expiration date).

As you probably know, the Fair Automobile Insurance Reform Act (FAIR Act) abolished the JUA and replaced it with the Market Transition Facility of New Jersey (MTF).

The FAIR Act also required private insurance companies to insure an increasingly larger share of New Jersey drivers. Under this program, private insurance companies had to insure 68 percent of all cars by October 1, 1990.

However, some companies did not write enough new policies by that 1990 deadline. As a result, these companies are being assigned drivers from the JUA and MTF.

As part of this program, your policy has been selected for assignment to (insert member company name). Some important facts about this assignment plan are:

1. (Insert member company name) must offer you the same or similar coverage as you have under your JUA policy. (Insert member company name) cannot offer you

less coverage. If the same or similar coverage is unavailable, (insert member company name) must offer you the next broadest coverage available.

2. If you accept this offer of coverage, (insert member company name) must insure you for a minimum of one year from (insert MTF policy expiration date), the expiration date of your MTF policy.

3. (Insert member company name) cannot cancel or nonrenew your policy during this one year period, except for nonpayment of premium.

4. You can ask (insert member company name) for additional coverage, less coverage, or other changes in your coverage. You may have to complete a Coverage Selection Form to make any changes in your coverage.

The enclosed offer is based on information sent to (insert member company name) by your MTF servicing carrier. Your premium may later change based on new information (for example, new car, new job, additional motor vehicle violations or accidents).

Please send your payment to (insert member company name) and not to your MTF servicing carrier. Be sure to include your name and new policy number on your check.

You may receive offers of coverage from other private insurance companies. You may shop around for coverage with another company on your own. **THE CHOICE IS YOURS.**

However, you must choose one of these offers of coverage or obtain coverage on your own because state law requires you to carry liability coverage.

Since you were assigned to (insert member company name), *you are not eligible to renew your policy with MTF.*

You should also know that under the FAIR Act you will have the right to buy insurance from the private insurance company of your choice beginning on April 1, 1992, if you have fewer than nine insurance points on your record. Please contact your insurance broker or the Public Affairs Division at the Department of Insurance if you have additional questions.

Please keep in mind that you are still represented by the same broker. Your broker is available to answer your questions and to advise you on your coverage.

Thank you for your cooperation.

- c: (Insert producer name)
(Insert producer business address)
(Insert producer telephone number, including area code)

EXHIBIT 3

(MEMBER COMPANY LETTERHEAD
INFORMATION GOES HERE)

(Insert mailing date of notice)

Newly Assigned Automobile Insurance Company:

(Insert member company name)

(Insert member company address, including city, state & zip code)

(Insert 800 toll free policyholder telephone number, if available, or New Jersey telephone number, including

area code, where policyholder can call for general information)

Previous Automobile Insurance Company:

Market Transition Facility of New Jersey (MTF)

Serviced by: (Insert name of MTF servicing carrier)

MTF Policy Number: (Insert MTF policy number)

MTF Policy Expiration Date: (Insert policy expiration date)

Policyholder:

(Insert name of policyholder)

(Insert policyholder's address, including city, state & zip code)

Dear Policyholder:

Your automobile insurance policy with the Market Transition Facility of New Jersey (MTF) expires on (insert MTF policy expiration date).

As you probably know, the Fair Automobile Insurance Reform Act (FAIR Act) abolished the New Jersey Automobile Full Insurance Underwriting Association (JUA) and replaced it with the MTF.

The FAIR Act also required private insurance companies to insure an increasingly larger share of New Jersey drivers. Under this program, private insurance companies had to insure 68 percent of all cars by October 1, 1990.

However, some companies did not write enough new policies by that 1990 deadline. As a result, these companies are being assigned drivers from the JUA and MTF.

As part of this program, your policy has been selected for assignment to (insert member company name). Some important facts about this assignment plan are:

1. (Insert member company name) must offer you the same or similar coverage as you have under your MTF policy. (Insert member company name) cannot offer you less coverage. If the same or similar coverage is unavailable, (insert member company name) must offer you the next broadest coverage available.

2. If you accept this offer of coverage, (insert member company name) must insure you for a minimum of one year from (insert JUA policy expiration date), the expiration date of your JUA policy.

3. (Insert member company name) cannot cancel or nonrenew your policy during this one year period, except for nonpayment of premium.

4. You can ask (insert member company name) for additional coverage, less coverage, or other changes in your coverage. You may have to complete a Coverage Selection Form to make any changes in your coverage.

The enclosed offer is based on information sent to (insert member company name) by your JUA servicing carrier. Your premium may later change based on new information (for example, new car, new job, additional motor vehicle violations or accidents).

Please send your payment to (insert member company name) and not to your JUA servicing carrier. Be sure to include your name and new policy number on your check.

You may receive offers of coverage from other private insurance companies. You may shop around for coverage with another company on your own. THE CHOICE IS YOURS.

However, you must choose one of these offers of coverage or obtain coverage on your own because state law requires you to carry liability coverage.

Since you were assigned to (insert member company name), *you are not eligible to renew your policy with the MTF.*

You should also know that under the FAIR Act you will have the right to buy insurance from the private insurance company of your choice beginning on April 1, 1992, if you have fewer than nine insurance points on your record. Please contact your insurance broker or the Public Affairs Division at the Department of Insurance if you have additional questions.

Please keep in mind that you are still represented by the same broker. Your broker is available to answer your questions and to advise you on your coverage.

Thank you for your cooperation.

c: (Insert producer name)
(Insert producer business address)
(Insert producer telephone number, including area code)

EXHIBIT 4

(MEMBER COMPANY LETTERHEAD
INFORMATION GOES HERE)

(Insert mailing date of notice)

Automobile Insurance Company

(Insert member company name)

(Insert member company address, including city, state & zip code)

(Insert 800 toll free policyholder telephone number, if available, or New Jersey telephone number, including area code, where policyholder can call for information)

Policyholder

(Insert name of policyholder)

(Insert policy number)

(Insert policyholder's address, including city, state & zip code)

IMPORTANT NOTICE

Thank you for choosing to be insured with (Name of Company). Our records indicate that you have not signed and returned the Coverage Selection Form sent to you with our (offer/policy). We need to have a copy of a signed Coverage Selection Form in our files. Therefore, another Coverage Selection Form and Buyer's Guide is enclosed with this Notice.

Please review the enclosed Coverage Selection Form. It is already filled in with the same or equivalent policy coverages and limits selections that you made for your JUA policy. *If you do not want to change the coverages or*

limits, simply sign the form and return it in the envelope provided.

If you wish to make changes in your policy coverages or limits, review the Buyer's Guide and/or consult with your producer and make changes to the Coverage Selection Form and return it in the envelope provided.

IF YOU DO NOT SIGN AND RETURN THIS COVERAGE SELECTION FORM, SOME OF YOUR COVERAGES WILL CHANGE AUTOMATICALLY AS DESCRIBED BELOW AND THESE CHANGES MAY NOT BE WHAT YOU DESIRE.

(1) You will receive the Lawsuit Threshold for Item 2; and

(2) If you have Collision and Comprehensive Coverages, you will receive the \$500 deductible unless the deductible on your JUA policy was higher.

To ensure that you have the policy coverages and limits that you want, please sign and return the Coverage Selection Form in the envelope provided. If you have any questions, please call your producer or our Customer Service representatives at the number listed above.

Thank you for your cooperation.

c: (Insert Producer Name)
(Insert Producer Business Address)
(Insert Producer Telephone Number, including area code.)

EXHIBIT 5

(MEMBER COMPANY LETTERHEAD
INFORMATION GOES HERE)

(Insert mailing date of notice)

Automobile Insurance Company

(Insert member company name)

(Insert member company address, including city, state & zip code)

(Insert 800 toll free policyholder telephone number, if available, or New Jersey telephone number, including area code, where policyholder can call for information)

Policyholder

(Insert name of policyholder)

(Insert policy number)

(Insert policyholder's address, including city, state & zip code)

IMPORTANT NOTICE

Thank you for choosing to be insured with (Name of Company). Our records indicate that you have not signed and returned the Coverage Selection Form sent to you with our (offer/policy). We need to have a copy of a signed Coverage Selection Form in our files. Therefore, another Coverage Selection Form and Buyer's Guide is enclosed with this Notice.

Please review the enclosed Coverage Selection Form. It is already filled in with the same or equivalent policy coverages and limits selections that you made for your MTF policy. *If you do not want to change the coverages or*

limits, simply sign the form and return it in the envelope provided.

If you wish to make changes in your policy coverages or limits, review the Buyer's Guide and/or consult with your producer and make changes to the Coverage Selection Form and return it in the envelope provided.

IF YOU DO NOT SIGN AND RETURN THIS COVERAGE SELECTION FORM, SOME OF YOUR COVERAGES WILL CHANGE AUTOMATICALLY AS DESCRIBED BELOW AND THESE CHANGES MAY NOT BE WHAT YOU DESIRE.

(1) You will receive the Lawsuit Threshold for Item 2; and

(2) If you have Collision and Comprehensive Coverages, you will receive the \$500 deductible unless the deductible on your MTF policy was higher.

To ensure that you have the policy coverages and limits that you want, please sign and return the Coverage Selection Form in the envelope provided. If you have any questions, please call your producer or our Customer Service representatives at the number listed above.

Thank you for your cooperation.

c: (Insert Producer Name)
(Insert Producer Business Address)
(Insert Producer Telephone Number, including area code.)

EXHIBIT 6

IBM STANDARD LABELS
 DCB INFORMATION
 RECORD FORMAT = VARIABLE BLOCKED
 BLOCKSIZE = 32760
 STREAMING TAPE DENSITY = 6250

<u>FIELD NAME</u>	<u>FIELD TYPE</u>	<u>FIELD LENGTH</u>
RECORD KEY		
POLICYHOLDER RECORD		
Producer Name		
Additional Producer Name	A/N	40
Producer Address	A/N	40
Additional Producer Address	A/N	40
Producer City-State-Zip	A/N	39
Policy Expiration Date	N	6
Policyholder Name	A/N	40
Additional Policyholder Name	A/N	40
Policyholder Address		
(Mailing)	A/N	40
Additional Policyholder		
Address (Mailing)	A/N	40
Policyholder City-State-Zip		
(Mailing)	A/N	39
Policyholder Rating Address	A/N	40
Additional Rating Address	A/N	40
Rating City-State-Zip	A/N	39
DRIVER RECORD (5)		
Driver Name	A/N	40
Driver License Number	A/N	22
State of License	A/N	2
Date of Birth	A/N	6
Driver Sex Code	A	1
Driver Marital Status	A	1
Date Licensed	N	6

DRIVER EVENT RECORD (5)

Driver Event Code	A/N	5
Driver Event Date	N	6
Event At-Fault Indicator	A	1
Total Points	N	2

DRIVER CLAIM RECORD (5)

Claim Date of Loss	N	6
Claim At-Fault Indicator	A	1
Claim Coverage Codes	A/N	8
Total Amount Paid	N	7
Date Paid	N	6
Accident Date	N	6
Claim Number	A/N	20
Comments	A/N	150

FOR MANDATORY ASSIGNMENT POLICIES

VEHICLE RECORD

Rating Territory	A/N	2
Garage Zip Code	N	5
Model Year	A/N	2
Vehicle Make/Model	A/N	17
Vin Number	A/N	17
Vehicle Type	A/N	1
Vehicle Symbol	A/N	2
Expiring Class Code	A/N	6
Vehicle Driver Date Of Birth	N	6
Anti-Theft Device Discount		
Percent	N	1
Passive Restraint Flag	A/N	1
Vehicle Stated Amount		
(Worth)	N	6
Driver Number	N	2
Principal Operator Indicator	A	1
Bodily Injury - Split	A/N	1
Bodily Injury - CSL	A/N	1
Property Damage	A/N	1
Medical Expense	A/N	1
Uninsured Motorist - Split	N	1

Uninsured Motorist - CSL	N	1
Uninsured Motorist - PD	N	1
UMPD Deductible	A/N	1
Tort Threshold	A/N	1
PIP Coverage	A/N	3
PIP Deductible	A/N	1
PIP Setoff Flag	A/N	1
Comprehensive Deductible	A/N	3
Collision Deductible	A/N	3
Rental Reimbursement	A	1
Non-Owned Coverage	A/N	2
Sound Tapes	A	1
Sound Equipment	A/N	1
Cost of Customization	N	6
LIENHOLDER NAME RECORD		
Lienholder Indicator	A/N	1
Lessor/Additional Insured Record	A/N	1
ASSIGNED COMPANY IDENTIFIER		
NAIC Company/Group Number	N	8

EXHIBIT 7

MANDATORY DEPOPULATION ASSIGNMENT PROGRAM MEMBER COMPANY MONTHLY REPORT

MEMBER COMPANY OR GROUP NAME:
(DATE OF REPORT)

FOR MONTH OF

NAIC NO.:

TOTAL NO. OF EXPOSURES ASSIGNED:

	# OF	CUMULATIVE	# OF	CUMULATIVE	# OF	CUMULATIVE	# OF	CUMULATIVE	# OF	CUMULATIVE	# OF	CUMULATIVE
	RECORDS	RECORDS	OFFERS	OFFERS	OFFERS	OFFERS	EXPOSURES	EXPOSURES	EXPOSURES	EXPOSURES	POLICIES	POLICIES
RATING	RECEIVED	RECEIVED	ISSUED	ISSUED	ACCEPTED	ACCEPTED	WRITTEN	WRITTEN	WRITTEN	WRITTEN	CANCELED/ NONRENEWED	CANCELED/ NONRENEWED
TERR. #	(FOR MO.)	(YR TO DATE)	(FOR MO.)	(YR TO DATE)	(FOR MO.)	(YR TO DATE)	(FOR MO.)	(YR TO DATE)	(FOR MO.)	(YR TO DATE)	(FOR MO.)	(YR TO DATE)

EXHIBIT 7

MANDATORY DEPOPULATION ASSIGNMENT PROGRAM MEMBER COMPANY MONTHLY REPORT

HER COMPANY OR GROUP NAME:
(OF REPORT)

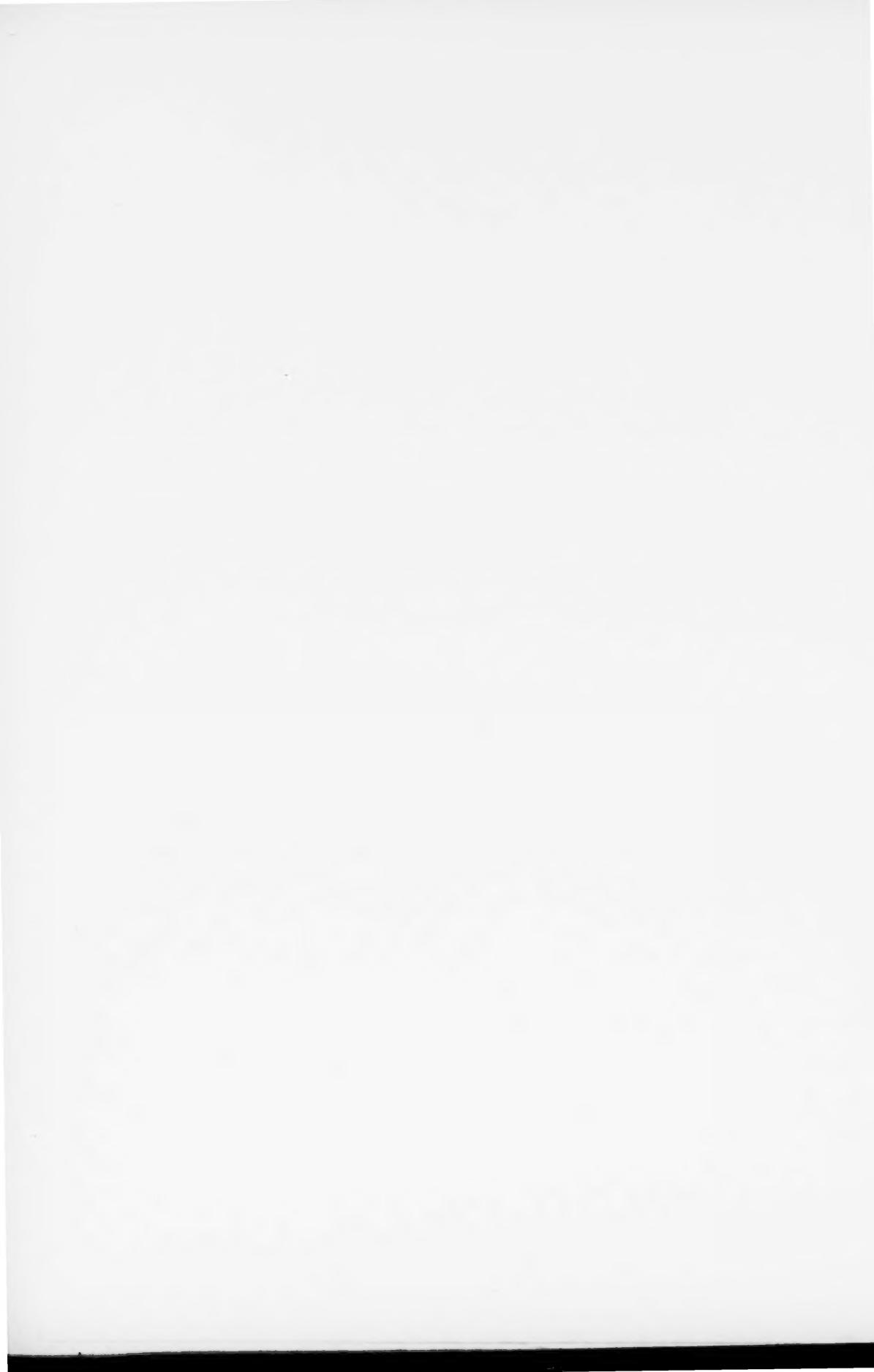
FOR MONTH OF

NAIC NO.:

TOTAL NO. OF EXPOSURES ASSIGNED:

	# OF	CUMULATIVE	# OF	CUMULATIVE	# OF	CUMULATIVE	# OF	CUMULATIVE	# OF	CUMULATIVE	# OF	CUMULATIVE
	RECORDS	RECORDS	OFFERS	OFFERS	OFFERS	OFFERS	EXPOSURES	EXPOSURES	EXPOSURES	EXPOSURES	POLICIES	POLICIES
RATING	RECEIVED	RECEIVED	ISSUED	ISSUED	ACCEPTED	ACCEPTED	WRITTEN	WRITTEN	WRITTEN	WRITTEN	CANCELED/ NONRENEWED	CANCELED/ NONRENEWED
TERR. #	(FOR MO.)	(YR TO DATE)	(FOR MO.)	(YR TO DATE)	(FOR MO.)	(YR TO DATE)	(FOR MO.)	(YR TO DATE)	(FOR MO.)	(YR TO DATE)	(FOR MO.)	(YR TO DATE)

TOTALS



APPENDIX 2

**In the Matter of the Assignment of Exposures to the
AETNA CASUALTY AND SURETY COMPANY, All-
state Insurance Company and Colonial Penn Insurance
Company.**

Superior Court of New Jersey, Appellate Division.

Argued March 6, 1991.

Decided May 20, 1991.

The opinion of the court was delivered by

COHEN, R.S., J.A.D.

Aetna, Allstate and Colonial Penn are insurers doing auto insurance business in New Jersey. On January 24, 1991, the Commissioner of Insurance ordered each of them to issue auto policies, commencing April 1, 1991, to thousands of "exposures" (private passenger cars requiring insurance) then insured in the "residual" market through the Joint Underwriting Association. The order was in furtherance of the phasing-out or "depopulation" of JUA undertaken by the Commissioner pursuant to the Fair Automobile Insurance Reform Act of 1990 ("FAIR Act"). L. 1990, c. 8. The initial set of orders went to 44 insurers and required coverage of some 211,000 exposures. We stayed the effect of the depopulation orders pending the appeals, consolidated them, and accelerated briefing and argument.¹ We now affirm the

¹ Colonial Penn Insurance Company had a special problem. It had an already-filed appeal pending in this court relating to the Commissioner's order establishing the conditions under which it would be permitted to withdraw from the New Jersey auto insurance market. One of those conditions was that withdrawal could take place only over a period of five years. During that time, Colonial Penn would be exposed to FAIR Act

(Continued on following page)

depopulation orders in part, but we invalidate them in part as unauthorized by the enabling legislation.

The setting is the perennially troubled New Jersey auto insurance market. The legislative highlights of the past twenty years start with the adoption in 1970 of the assigned risk plan, which authorized the forced distribution among insurers of auto insurance applicants who were unable to procure coverage "through ordinary methods." *N.J.S.A. 17:29D-1*. Effective on January 1, 1973, was the New Jersey Automobile Reparation Reform Act, *N.J.S.A. 39:6A-1 et seq.*, which made auto insurance compulsory and created extensive no-fault benefits but imposed a tort suit threshold that barred very few tort suits. *See also N.J.S.A. 39:6B-1*.

In 1983 appeared the New Jersey Automobile Full Insurance Availability Act, *N.J.S.A. 17:30E-1 et seq.*, whose purpose was to supplant the assigned risk system and "to assure to the New Jersey insurance consumer full access to automobile insurance through normal market outlets at standard market rates, . . . and to require that companies be made whole for losses in excess of regulated rates on all risks not voluntarily written. . . ." *N.J.S.A.*

(Continued from previous page)

obligations for the depopulation of JUA and the satisfaction of JUA deficits. We consolidated Colonial Penn's appeal from the January 24 depopulation order to the extent that it raised issues other than those arising out of its status as a withdrawing insurer, leaving the latter issues for consolidation with its already-filed appeal of the Commissioner's withdrawal order.

17:30E-2. Unlike the assigned risk system, the new legislation contemplated coverage provided by JUA, at standard market rates, to risks rejected by the voluntary market. Although policies were to be issued in the names of servicing insurers, the risks would be borne by JUA, and servicing insurers would be paid fees for handling coverage, premiums and claims. JUA's underwriting losses, which were inevitable, would be made up from bad-driver and accident surcharges imposed by the Division of Motor Vehicles and JUA, and the "residual market equalization charge" ("RMEC"), which was to be levied equally on all autos insured in the voluntary and residual markets except those with principal drivers aged 65 years or older. *N.J.S.A. 17:30E-8b. See Senate Labor, Industry and Professions Committee Statement, Assembly, No. 1696-L. 1983, c. 65. The RMECs were to be sufficient to permit JUA to operate on a no-profit, no-loss basis. N.J.S.A. 17:30E-3o.*

In 1988, amendments to various statutes were made to correct deteriorating conditions in the auto insurance industry. Insurers were more and more restricting their voluntary coverage to the most favorable risks, leaving fully half of the State's drivers to be covered through JUA at artificially low rates. JUA was experiencing constantly worsening imbalances, and was kept afloat by increasingly large charges imposed on all New Jersey drivers. *See Governor's Reconsideration and Recommendation Statement, Senate No. 2637-L. 1988, c. 119. Blame was variously assigned by various people. It was the over-generous no-fault law. It was the refusal of the Commissioner of Insurance to permit insurers to earn an*

adequate rate of return on voluntary business. It was the refusal of insurers to provide coverage to urban drivers

The new statutes introduced an optional verbal threshold for tort actions, *N.J.S.A. 39:6A-8, 8.1*; flex-rating for insurers, *N.J.S.A. 17:29A-44*; an insurers' excess profits law, *N.J.S.A. 17:29A-5.6 et seq.*; 10% annual increases in JUA rates for bad drivers for four years, *N.J.S.A. 17:30E-13a through d*, an authorization for deferral of JUA payments of bodily injury losses when JUA's income is insufficient to meet its obligations, *N.J.S.A. 17:30E-8.1*; an authorization for a multi-tier rating system in the voluntary market, including rates for good drivers and substandard risks, *N.J.S.A. 17:29A-45*; and a requirement for the audit of servicing carriers to find and recover overcharges resulting from their claims practices, and treble damages for wilful overcharges. *N.J.S.A. 17:30E-17.1*. See Senate Labor, Industry and Professions Committee Statement, Assembly No. 3702-L. 1988, c. 156.

Perhaps the most important aspect of the 1988 legislation was a scheme for the downsizing, or depopulation, of JUA over a four-year period, to the end that it would serve only its original purpose of providing insurance coverage for the least desirable risks. *N.J.S.A. 17:30E-14*. Those residual risks would be charged self-sustaining rates, which would not be subsidized by the voluntary market. The statute directed the Commissioner to establish procedures to govern the voluntary market's² writing

² The 1988 and 1990 legislation is full of references to compulsory measures to be applied to the "voluntary" market.

(Continued on following page)

of JUA insureds and applicants for insurance. In annual increments, the voluntary market insurers were to increase the percentage of private passenger car exposures they insured in the voluntary market from 50% to 60%, then 70%, 75% and 80%. Methods were prescribed for apportioning and assigning to voluntary market insurers the number of JUA insureds sufficient to make up any shortfall that occurred in the required annual increase in voluntarily written policies.

On March 12, 1990, the FAIR Act became law, effective immediately. It attacked most of the same problems to which the 1988 legislation was addressed. It did so, however, in a more urgent and drastic manner. One of the elements of the FAIR Act was the imposition on the voluntary market of surtaxes and assessments to satisfy the \$3.3 billion of accumulated obligations of JUA.³ Fees

(Continued from previous page)

An example is the obligatory "voluntary market quota" in N.J.S.A. 17:30E-14b(1). The only way for the reader to avoid constant surprises is to read the word "voluntary" without attaching any connotation of free will.

³ For a discussion of the impact of the surtaxes and assessments on the ratemaking process, see our recently filed *Allstate Ins. Co. v. Fortunato*, 248 N.J. Super. 153, 590 A.2d 690 (App.Div.1991). The statute prohibits a carrier to pass through the amount of the surtaxes and assessments in premium increases. The facial constitutional validity of the prohibition was upheld in *State Farm Mut. Auto Ins. Co. v. Fortunato*, 124 N.J. 32, 590 A.2d 191 (1991), in the light of the constitutional, statutory, and regulatory entitlement of the insurers to an adequate rate of return.

to be collected from doctors, lawyers, and auto body shops were also devoted to the same purpose. *N.J.S.A.* 17:33B-58 to 63. Most importantly, the Legislature abandoned JUA as a continuing insurance market mechanism.

The function of JUA was turned over by the statute to the Market Transition Facility ("MTF"). MTF was expected to operate from October 1, 1990 to September 30, 1992, when it would go out of business. Premiums on policies issued by MTF were initially to be based on September 30, 1990 JUA rates. *N.J.S.A.* 17:33B-11. No RMECs, however, were to be charged after April 1, 1991. The loss of MTF support would have to be made up from other sources. MTF's profits and losses were to be apportioned among the auto insurers. *N.J.S.A.* 17:33B-11d. It was expected that JUA's business would already have decreased to 40% of the total private auto market under the 1988 legislation, and then to 32% soon after enactment of the 1990 FAIR Act. By April 1, 1991, only 29% of the market was to be covered by MTF; by October 1, 1991, 20%, and by April 1, 1992, 10%. MTF was to write no new business after October 1, 1992, after which exposures rejected by the voluntary market would be relegated to the assigned risk plan. *N.J.S.A.* 17:33B-11c(5); 17:29D-1.

It was pursuant to the 1990 FAIR Act that the Commissioner promulgated his January 24 depopulation orders. There were 44 orders issued, one to every insurer that failed to meet its share of the first stage of distribution of JUA insureds to the voluntary market. There were 24 other insurers that had already met their quotas, and therefore avoided the obligation to accept further exposures to satisfy the goal of reducing the portion of the

auto insurance market covered by JUA/MTF. The appellants suspect that these 24 insurers made their quotas by "cherry-picking" the least-risk JUA/MTF insureds. That may be so. If it is, the appellants had the same opportunity, and apparently chose not to utilize it.

The insurers raised various objections to the orders. Our approach to each of the issues presented by these appeals is governed by some basic principles. It is clear that the insurance industry is strongly affected with a public interest, and is therefore properly subject to comprehensive regulation to protect the public welfare. *Sheeran v. Nationwide Mut. Ins. Co.*, 80 N.J. 548, 559, 404 A.2d 625 (1979). The Legislature has broad discretion in adopting police power regulations governing the insurance business to promote what the Legislature views as the public interest. This includes the power to compel insurers to cover people they would rather not insure. *California State Auto. Ass'n Inter-Ins. Bur. v. Maloney*, 341 U.S. 105, 71 S.Ct. 601, 95 L.Ed. 788 (1951). It also includes requiring insurers to renew policies they would like to drop. *Sheeran, supra*, 80 N.J. at 560, 404 A.2d 625. The State's broad regulatory powers must be exercised, however, so as to allow insurers a fair and reasonable return. *Id.*

Administrative actions, such as the Commissioner's depopulation orders, must be upheld unless they exceed his statutory authority, or are arbitrary, capricious or unreasonable. *Henry v. Rahway State Prison*, 81 N.J. 571, 579-580, 410 A.2d 686 (1980). The burden is on the objector to overcome the presumption that agency actions are valid and reasonable. *Medical Soc'y of New Jersey v. New Jersey Dept. of Law and Public Safety*, 120 N.J. 18, 25, 575

A.2d 1348 (1990). The Commissioner's expertise in the field of insurance must be given great weight. *IFA Ins. Co. v. New Jersey Dept. of Ins.*, 195 N.J.Super. 200, 206-207, 478 A.2d 1203 (App.Div.), *certif. denied*, 99 N.J. 218, 491 A.2d 712 (1984).

I.

The insurers' first objection was that the depopulation orders assigned JUA/MTF exposures that were not eligible under the FAIR Act for assignment to the voluntary market. They argued that the depopulation orders made assignments of the entire books of business of producers⁴ in particular territories without regard to the likelihood that the books contain individual risks so substandard that they must ultimately be in the 10% that will be relegated to the assigned risk pool after MTF completes its transitional function. The Commissioner conceded that he included such risks in his orders, but argued (a) that § 20 of the FAIR Act permitted him to determine that all drivers would be eligible, (b) that it was utterly impractical for him to weed out the worst risks, and (c) that assigning only good drivers and keeping the bad in MTF would be unfair to other MTF insureds and would improperly reward insurers who did not meet their voluntary depopulation quotas and therefore had to accept assignments.

⁴ A producer is a licensed agent or broker, N.J.S.A. 17:30E-3(l).

N.J.S.A. 17:33B-13 contains a definition of "eligible person." In general, it is a person who has not given any of the seven listed indications of presenting an enhanced insurance risk, such as accidents, criminal convictions, and an accumulation of auto insurance eligibility points. However, the definition expressly applies only to a listed group of statutory provisions that deal with post-MTF eligibility for the voluntary market. FAIR Act § 20, *N.J.S.A. 17:30E-14*, is not one of those provisions. *N.J.S.A. 17:30E-14* was a part of the 1988 legislation and survives as amended in 1990. *N.J.S.A. 17:33B-13* was newly enacted in 1990. *N.J.S.A. 17:30E-14* authorizes the Commissioner to develop "criteria identifying drivers who should be eligible for coverage in the voluntary market," and to make assignments of people meeting those criteria. The Commissioner argued in briefs before us that the *N.J.S.A. 17:33B-13* definition does not control, and that it was permissible for him to exercise his judgment to determine that every person insured by JUA/MTF was eligible for the voluntary market for the purpose of the depopulation orders.

At oral argument before us, for reasons not explained, the Commissioner announced that he had changed his mind. His new position was that he agreed with the insurers that they should have to provide coverage only for exposures that would be considered eligible under *N.J.S.A. 17:33B-13*. He added, however, that the insurers would have to investigate and identify the ineligible assigned to them, and he would not afford them sufficient time to do so before their coverage obligation attached. That position created the serious question whether the insurers would thereafter be permitted to

shed the insureds they discovered were ineligible after initiating coverage.

Because we sensed that an equitable accommodation could be reached, we gave the parties time to confer. They ultimately arrived at a solution which gave the insurers the burden of identifying ineligible exposures, but which also gave them sufficient time to permit them to withhold offering coverage to ineligible and to permit the ineligible to remain MTF insureds.

The issue of eligibility was thus equitably and sensibly resolved by the parties. We describe the dispute, and the manner in which the confrontation was dissolved, for a purpose. It is to put other disputes raised before us in better perspective. It is also to demonstrate that a more deliberate process of legislative enactment and administrative implementation could have prevented the actors from feeling obliged to take sword's point litigation postures on a number of matters having sensible and reachable solutions.

II.

N.J.S.A. 17:30E-14a instructs the Commissioner to establish "an equitable apportionment procedure" for the assignment of JUA/MTF insureds to insurers who fail to meet their periodic quotas. What the Commissioner did in the present group of depopulation orders was to distribute first the JUA/MTF insureds from those geographical territories in which the voluntary market covered the lowest percentages of the total exposures. Those territories are urban and economically depressed areas where, according to the insurers, a disproportionate number of

high-risk insureds are located. In addition, they argue, New Jersey's capped premium rates are purposely set at levels insufficient to reflect the extent of the risks actually incurred in covering inner city insureds. Selecting those least favored risks for assignment has the effect, according to the insurers, of imposing on them the penalty of writing the greatest-loss policies after other insurers have skimmed the cream of the JUA/MTF exposures. Instead, the exposures to be assigned in the depopulation orders should have been chosen at random from the entire list of eligible JUA/MTF exposures, without regard to territory. Only by that means, according to the insurers, could an equitable apportionment have been made.

There are a number of answers. The first is that the facts have changed since the insurers developed their argument. The change is the significant one of the Commissioner's agreement to let them delete from the depopulation orders the drivers deemed ineligible under *N.J.S.A. 17:33B-13*. The second answer is that The FAIR Act permits insurers taking on the coverage of assigned exposures to charge them MTF premium rates, which are higher than the voluntary market rates. *N.J.S.A. 17:33B-12*. The MTF rates will be even higher for bad drivers. *N.J.S.A. 17:29A-35*. The prospect of taking on bad risks at low rates is therefore not as dire as the insurers contend. The third is that every insurer had the opportunity to "cherry-pick", that is, each of them has known for many months the number of JUA/MTF exposures it had to take on in order to avoid assignments in the depopulation orders. Some insurers chose to reach out to add to their share of the market. Others chose not to do so. The "equitable apportionment" of exposures is

not necessarily achieved by placing insurers that have chosen to remain part of the problem on a par with insurers that have come forward to participate in the solution.

The fourth answer is that equity among insurers is not the only equity that legitimately concerned the Legislature and the Commissioner. The plain fact is that urban auto owners have not had fair access to the voluntary auto insurance market in recent years. The result is that great numbers of perfectly sound drivers have been relegated to JUA coverage. Perhaps it is because insurers abandoned the inner cities for profitable suburban business, without distinguishing good urban drivers from bad, as the Commissioner contends. Perhaps it is because the State did not permit the insurers to write inner city business without incurring substantial and irremediable losses, as the insurers reply. The early assignment of urban exposures in the depopulation process serves to give good urban drivers the same access to the benefits of the voluntary market as their suburban counterparts. Those benefits include a greater choice of benefits and carriers, and, eventually, of costs.

The choice the Commissioner made responds to legitimate legislative concerns in a reasonable way that does not unfairly prejudice the insurers. In these circumstances our responsibility is not to interfere.

III.

The insurers next argue that the feature of the depopulation orders assigning producers to the insurers with their books of business directly contravenes the

letter and spirit of *N.J.S.A. 17:30E-14i(3)*. The Commissioner argues that the assignment of producers is a legitimate effort on his part to effectuate the legislative will as derived from harmonizing *N.J.S.A. 17:30E-14i(3)* with *N.J.S.A. 17:33B-9c*, both of which deal with the role of JUA/MTF producers during and after the process of depopulation.

N.J.S.A. 17:30E-14i(3) is a part of the 1988 legislation that first approached the subject of downsizing JUA. It deals with the procedures to that end which the Commissioner was told to develop. It provides that those procedures shall

neither prohibit nor require member companies to write association business through association producers of record, provided, however, that where a member company elects not to service such business through the association producer of record, the procedures shall address the manner in which the association shall transfer the business to the member company, and shall establish reasonable compensation in an amount sufficient to offset the actual expenses incurred by the association producer in conjunction with the transfer which shall be paid by the association upon transfer of the business to the member company;

As we understand the provision, it says that an insurer taking on former JUA exposures as part of the depopulation plan may continue to write the business through the JUA producer who has been writing it, but need not do so

if it does not want to. If the insurer chooses not to write the business through the JUA producer, JUA transfers the exposure to the assigned insurer, and JUA pays the producer for the actual expenses of transfer. Even though the quoted language was part of the 1988 legislation, it appears as a part of § 20 of the FAIR Act, which is the section that amends the 1988 legislation to shorten the time periods for depopulation increments. It would be impossible in those circumstances to disregard the language, as the Commissioner says we should, as "a remnant" of earlier legislation which somehow slipped into the new law. We cannot assume that the Legislature did not know what it was enacting.

N.J.S.A. 17:33B-9c is new language in the FAIR Act, and is therefore, according to the Commissioner, the current legislative expression of policy. It says:

The commissioner shall, on or before October 1, 1991, establish a producer assignment program. The program shall be available upon application to any licensed insurance producer who: (1) is a producer for the association; (2) has no affiliation with a voluntary market company for the purposes of placement of private passenger automobile insurance; (3) had an affiliation with an insurance company for the placement of automobile insurance in the voluntary market which was terminated by the insurer on or after December 31, 1980; (4) has demonstrated to the commissioner his competency, efficiency and effectiveness in servicing association and other insurance business as determined by a review of the record of the producer for complaints,

violations of the licensing law and other factors deemed relevant by the commissioner; and (5) is located and services insurance in a geographic area which the commissioner has determined to lack sufficient representation for the placement of automobile insurance business in the voluntary market. The program shall provide for the assignment of qualified producers on an equitable basis to insurers writing private passenger automobile insurance in the voluntary market.

As we understand this provision, it is intended to create a post-October 1, 1991 assignment program for certain JUA/MTF producers who wish to participate, and who meet five listed criteria. Among them are that the producer has no affiliation with a voluntary market insurer, and that the producer is located and services insurance in a geographical area which the Commissioner determines has insufficient representation in the voluntary market. The Commissioner is directed to establish a program by October 1, 1991, to assign qualified producers on an equitable basis to voluntary market insurers. He has not yet done so. He has not determined whether the producers assigned to insurers in the January 24 depopulation orders would qualify for assignment under his yet-unestablished program.

The goal of the assignment program is to protect producers who have built businesses and developed insurance expertise writing JUA/MTF policies, and at the same time to encourage an auto insurance sales and service presence in underserved urban areas. The goal of N.J.S.A. 17:30E-14i(3), on the other hand, is to permit

voluntary market insurers to accept JUA/MTF assignments of exposures and service them through their own existing organizations, but with JUA/MTF providing compensation for transfer expenses to the affected producer. Aetna, for instance, intends to direct-write its assigned business. Colonial Penn does business only by direct writing.

The Commissioner argues that he "harmonized" the two statutory sections by assigning producers so that they will be able to survive until the October 1 assignment program has been established.⁵ Otherwise, he says, the program will be ineffective because the producers will have gone out of business.

It may well be that the producers would experience a lesser impact from the depopulation of JUA/MTF if the assignment of any of their business to the voluntary market had to include them as producers. But that would not justify our ignoring the plain words of *N.J.S.A. 17:30E-14i(3)*, words that were enacted only in 1988 and repeated in the FAIR Act in 1990. They flatly prohibit requiring voluntary market insurers to write assigned JUA/MTF business through the former producer of the business, or requiring the insurers to compensate the producers. If there is a discontinuity in the legislation, the Legislature can correct it in short order if it chooses to do

⁵ Before us, the Commissioner announced that his assignment of producers would be for one year only, a limitation not contained in the January 24 depopulation orders. The change is not material to the legal problem before us.

so. But, the Commissioner may not ignore the statute in the name of "harmonization."

IV.

Next, the insurers complain about that part of the depopulation orders that require them to cover the assigned exposures for a full year. Many insurers write six-month policies in their voluntary market business, without any objection from the Commissioner. They argue that they should be able to fold the assigned business into their established practices, and write six-month policies for their newly assigned business.

This is a matter which the Commissioner's judgment should control. He is dealing with the transfer to the voluntary market of hundreds of thousands of exposures. There will inevitably be disruption and inconvenience to everyone involved. In requiring full-year policies, the Commissioner sought to achieve in at least one manageable area a degree of uniformity and predictability. The means seem suited to achieve the desired end. The insurers' understandable concern is their own business convenience, but there is no legal entitlement to write six-month policies, and no real prejudice in being barred from doing so. In this respect, the Commissioner's orders are affirmed.

V.

The insurers also object that the orders unlawfully require them to offer to insure a substantially greater

number of exposures than necessary to meet their individual depopulation shortfalls. This is another issue that time seems to have resolved.

The Mandatory Depopulation Assignment Plan stated that the assignments to each insurer would be increased by an "acceptance factor" of 25%. The actual language was:

The number of exposures assigned to each member company shall be increased by an acceptance factor of 25 percent. It is the expectation of the Department that not every offer of coverage made by a member company to its assigned policyholders will be accepted. This expectation is based on the dynamic aspect of the New Jersey automobile insurance market (i.e. Association or MTF policyholders independently seeking coverage with a voluntary insurer, competition among member companies to write additional new business in order to meet future depopulation quotas, and Association or MTF policyholders leaving New Jersey).

* * *

The member company must continue to make offers of coverage to all assigned . . . policyholders even when the member company has written sufficient exposures to meet its apportionment share shortfall. Any exposures written in excess of the apportionment share shortfall may be used by the member company toward the fulfillment of its next apportionment share.

Two things developed while the appeals were before us. The first was that the increase of 25% was never applied to the insurers involved in these appeals. For a

reason not revealed to us, Aetna was not assigned an extra 25% of its shortfall but only an extra 7%. The Commissioner's brief justified the 7% excess on the unsupported thesis that "the industry norm for non-selection of renewals by the insured is 5-10%." Allstate, on the other hand, received an assignment of 94% of its shortfall. Colonial Penn received 99% of its shortfall. It has never been explained to us how the urgent reasons earnestly recited for the original decision to assign a 25% excess have dissipated.

It is apparent that the percentage differences among the assignments is accounted for by the Commissioner's decision to assign exposures in blocks consisting of producers' entire books of business. Since the Commissioner and the insurers have now decided that only eligible persons under *N.J.S.A. 17:33B-13* will be assigned, the number of exposures in a producer's book of business cannot be used as an accurate measure for assignment. In addition, since we have decided that producers may not lawfully be assigned to the voluntary market insurers with their books of business, there is much less reason to make assignments by use of producers' books, even after culling out the ineligible.

For those reasons there is no purpose in our ruling on the legality of a depopulation order provision which the Commissioner has apparently abandoned and which, in any event, is no longer justifiable even as a convenience.

VI.

Allstate argues that the Commissioner made "retro-active" changes in the depopulation procedures that

"unjustly impact Allstate." The reference is to the formula by which the quota of each insurer was to be calculated and the manner by which exposures were to be selected for assignment. Allstate contends that it made underwriting decisions in reliance on the depopulation plan adopted by the Commissioner before the FAIR Act (1) to use a 50-50 weighting of insurers' 1983 and 1988 voluntary business in the quota formula, and (2) to make assignments on a random basis. After those decisions were made, the Commissioner changed the ground rules by amending the formula to use a 75-25 weighting of the insurers' voluntary 1983 and 1988 business, thereby discounting recent shrinkage of an insurer's voluntary business,⁶ and by deciding to assign JUA/MTF exposures by territory and without regard to statutory eligibility. "Obviously," Allstate argues, "had Allstate known in a timely fashion that its obligations to insure former JUA insureds would be retroactively enlarged to require insurance of more exposures, to exclude any eligibility criteria in the assignment process, and to selectively assign from the most underpriced territories, Allstate would have expanded its underwriting guidelines and made targeted sales efforts so as to enable it to initially insure more of the better JUA risks, avoiding the need to later accept the worst of these risks."

⁶ Colonial Penn attacks the 75-25 weighting on the basis of its impact on a withdrawing insurer whose 1988 business was a fraction of its 1983 business. We do not foreclose Colonial Penn from making this argument in its appeal from the Commissioner's order establishing conditions for withdrawal.

There are a number of sound answers. The first is that Allstate does not demonstrate in any way what makes it obvious that it would have made consequential changes in underwriting or in corporate strategy. Skimming the cream from JUA was always encouraged by the depopulation plans. The only effect of the changes was to make skimming an even better idea. The second is that the problem of the assignment of ineligible risks has been resolved in Allstate's favor by the Commissioner. The third is that it is sensible to give 1983, the last year before the voluntary market had JUA available as a dumping ground for undesirable risks, three times the weight as 1988, the fifth year of JUA operation, when it had absorbed fully half of New Jersey's drivers. The fourth is that the challenged changes in the Commissioner's approach to the pressing problems he faced were responsive to the urgency displayed by both the letter and the spirit of the FAIR Act. In sum, Allstate has not shown either that it did in fact rely on the 1989 plan, or that such reliance was justified, detrimental and such as to create a protectible interest against change. Thus, we need not rule on the appropriateness of estoppel as a remedy for changing administrative action.

VII.

Finally, all of the insurers argue that it is unconstitutional for the Commissioner to implement the depopulation plan because (a) they are operating at a loss in their New Jersey auto insurance businesses, (b) the Commissioner is purposely and unlawfully delaying consideration of rate filings they have made seeking necessary premium increases, and (c) as things now stand, they will

inevitably lose money on the new business that the Commissioner proposes to assign them.

The parties do not disagree about the law applicable to this issue. The insurers are entitled to earn a reasonable rate of return on their New Jersey auto insurance business. *Sheeran, supra*, 80 N.J. at 560, 404 A.2d 625. The return should be one which is generally commensurate with returns on investments in other enterprises having comparable risks. *State Farm Mut. Auto Ins. Co. v. State of New Jersey*, 124 N.J.32, ___, 590 A.2d 191 (1991). There is no right to make money on every policy written, or on every day of business. There is, however, a right to have the regulatory agency which exercises the rate-making function do its job reasonably promptly, and with no more delay than is necessarily involved in the review process itself. *Helmsley v. Borough of Fort Lee*, 78 N.J. 200, 226-230, 394 A.2d 65 (1978), *appeal dismissed*, 440 U.S. 978, 99 S.Ct. 1782, 60 L.Ed.2d 237 (1979). The prime reason for expecting prompt consideration of rate increases is that they are prospective only. *Petition of Elizabethtown Water Co.*, 107 N.J. 440, 452-459, 527 A.2d 354 (1987). Thus, rates that were inadequate during a prolonged review process cannot be retroactively increased or otherwise made up.⁷ In addition, the insurers argue that, although a certain period of regulatory lag is unavoidable, it is one thing to

⁷ Board of Public Utilities statutes and regulations deal with the problem of regulatory lag by permitting implementation of interim rates, subject to rebate. See *In re Revision of Rates, Toms River Water Co.*, 82 N.J. 201, 208-212, 412 A.2d 430 (1980).

ask insurers to continue writing insurance they voluntarily contracted for while proposed rate hikes are carefully examined, but it is altogether another thing to coerce insurers to take on new business they do not want, at currently inadequate rates, and tell them to be patient while their requests for adequate rates wend their way through the regulatory process.

What the parties disagree about, at the tops of their voices, are the facts. The record before us is full of significant and irreconcilable factual differences. The insurers offer complex financial analyses and the assurance of their actuaries and executives that they are losing millions of dollars on their current New Jersey business. They say the near future promises even greater losses with or without their assigned JUA/MTF business, that the Commissioner is dragging his feet in considering their rate filings, and that forcing more business on them at insufficient rates is confiscatory. The Commissioner offers equally complex analyses and the assurance of his actuaries that the insurers are really doing just fine, and that their complaints are baseless.

The insurers and the Commissioner not only disagree on the facts. They also accuse each other of bad faith, and describe each other's motives as unworthy, tactics as inappropriate, and goals as improper. There is a counter-productive air of distrust and hostility that surrounds the subject and displaces reasonable discussion.

However good the insurers' evidence may be of currently insufficient rates on their voluntary business, that evidence does not bear directly on the economic impact of their taking on JUA/MTF exposures. One reason is

that they have rate filings pending which could result in higher revenues. Another reason is that they need not charge their voluntary market rates to the exposures they are assigned. Instead, they can charge MTF rates. Current MTF rates are higher than the current voluntary market rates of Aetna and Allstate, and, we assume, also of Colonial Penn. In addition, MTF rates will be supplemented for substandard drivers who are still eligible for assignment. The supplement may not be as great as the insurers think will be necessary, but that is very difficult to evaluate now. Moreover, MTF has already applied to the Commissioner for a 28% rate hike, approval of which would further increase premium levels. Not enough, say the insurers, pointing out that MTF has announced that its rates need a 60% increase to permit MTF to break even; insurers are entitled to earn a profit, and MTF's break-even rates are therefore inadequate by definition.⁸

The insurers do not make a case of sufficient strength to justify our entering an order freezing in place a currently disastrous insurance industry situation until the insurers' hyperbole can be tested against the Commissioner's incredulity. The resulting turmoil in the State's auto insurance industry would be intolerable.

The insurers suggest another possibility, which is that the depopulation process proceed with the Commissioner's permitting them to charge interim enhanced premium rates on assigned exposures, the excess of which

⁸ We understand that, after oral argument before us, the Commissioner completed his review of MTF's rate filing and has granted some but not all of the rate relief MTF sought. We cannot evaluate the impact of his decision on these parties.

would be escrowed by the insurers until all of the relevant rate filings have been considered and approvals made to raise voluntary market and MTF rates to a level at which the insurers will be able to earn an adequate return.

The Commissioner replies that he has no power to approve interim rates with effective consumer protections against overcharges. We need not resolve that dispute. Cf. *New Jersey St. AFL-CIO v. Bryant*, 55 N.J. 171, 260 A.2d 225 (1969).

The insurers will be able to charge the recently enhanced MTF rates to their assigned exposures. That creates a better situation than was predicted for the insurers at the time of their briefs and oral arguments. Whether it is better enough would no doubt be the subject of some disagreement. We are in no position, however, to predict whether that untested new business taken on by the insurers from MTF at untested new MTF premium rates will result in future losses so clear and significant that the insurers are entitled to protection in advance.

Except as to the provision for the assignment of producers and those matters which we have said have been resolved without our decision, *i.e.*, the assignment of ineligibles and the assignment of an excess of 25% of quota, the January 24, 1991 depopulation orders of the Commissioner are affirmed.

APPENDIX 3

SUPREME COURT
OF NEW JERSEY
C-73 September Term 1991

33,829

IN THE MATTER OF THE
ASSIGNMENT OF
EXPOSURES TO THE
AETNA CASUALTY AND
SURETY COMPANY,
ALLSTATE INSURANCE
COMPANY AND
COLONIAL PENN
INSURANCE COMPANY,

ON PETITION
FOR CERTIFICATION
(Filed Sept. 18, 1991)

(Allstate Insurance Company – Petitioner)

To the Appellate Division, Superior Court,

A petition for certification of the judgment in
A-2628/2631/2783-90T5 having been submitted to this
Court, and the Court having considered the same;

It is ORDERED that the petition for certification is
denied, with costs; and it is further

ORDERED that the appeal in the within matter is
dismissed pursuant to R. 2:12-9.

WITNESS, the Honorable Robert N. Wilentz, Chief
Justice, at Trenton, this 16th day of September, 1991.

I hereby certify that the
foregoing is a true copy of
the original on file in my
office.

/s/ Stephen W. Townsend
CLERK OF THE
SUPREME COURT
OF NEW JERSEY

/s/ Stephen W. Townsend
CLERK OF THE
SUPREME COURT

APPENDIX 4

IN THE MATTER OF THE	) SUPREME COURT OF
ASSIGNMENT OF	) NEW JERSEY
EXPOSURES TO	) DOCKET NO.
THE AETNA CASUALTY	) <u>CIVIL ACTION</u>
AND SURETY)
COMPANY, ALLSTATE	) ON PETITION FOR
INSURANCE COMPANY	) CERTIFICATION
AND COLONIAL	) OF FINAL JUDGMENT OF
PENN INSURANCE	) NEW JERSEY SUPERIOR
COMPANY.	) COURT, APPELLATE
	) DIVISION
	) Sat Below: Judges Long,
	) Cohen and
	) Stern, J.A.D.
)
	) (Filed July 9, 1991)
	) SUPREME COURT OF
	) NEW JERSEY

PETITION FOR CERTIFICATION AND APPENDIX
OF ALLSTATE INSURANCE COMPANY

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PRELIMINARY STATEMENT

The Automobile Full Insurance Availability Act of 1983 ("JUA Act"), N.J.S.A. 17:30-1 *et seq.*, created the New Jersey Automobile Full Insurance Underwriting Association (the "JUA") to insure, at voluntary-market rates, drivers whom private insurers were not willing to insure at those rates. In 1988, the Legislature sought to "depopulate" the JUA, which had at that point grown to approximately 50% of the New Jersey automobile insurance market, by establishing a series of increasing percentages of vehicles in the State which must be insured in the voluntary market. N.J.S.A. 17:30E-14.

The Commissioner of Insurance ("Commissioner") was required to establish standards for apportioning industrywide depopulation obligations among these insurers and for assigning JUA insureds to private insurers if the required percentages of vehicles had not been insured. Because of the JUA's inadequacies, the Fair Automobile Insurance Act of 1990 ("FAIRA") abolished the JUA, temporarily transferred the JUA's remaining business to the Market Transition Facility ("MTF") and accelerated the contemplated depopulation of the JUA/MTF into the private market.

Allstate Insurance Company ("Allstate") seeks certification from a judgment of the Appellate Division upholding, in relevant part, an order ("Depopulation Order" or "Order") issued by the Commissioner requiring Allstate to offer insurance for approximately 30,000 vehicles now insured by the MTF, which is the statutory successor to the JUA.

No adequate rates have ever been set for this compelled business. Nor has a proceeding been held which would allow Allstate to charge such adequate rates. As a result, Allstate showed that, at the rates in effect at the time of the Depopulation Order, it would suffer an annual operating loss on depopulation business of approximately \$20 million and that no excess profits were available from its other business to absorb that loss. (Allstate Appellate Division Appendix ("ALa") 43a-45a) Current rate inadequacies cannot be recouped in the setting of future rates, so the Depopulation Order presents a clear risk of irreparable harm to Allstate's statutory and constitutional rights not to suffer confiscation of its property. The Commissioner and the Appellate Division have refused to protect Allstate against this risk of irreparable harm pending determination of the proper rates.

The Order also requires Allstate to accept a disproportionate number of depopulation assignments from the New Jersey territories where, due to limitations on geographic rate differentials, the rates are the most inadequate. That method of assignment violates the statutory requirement that depopulation assignments be made in an "equitable" fashion.

STATEMENT OF MATTER INVOLVED

This case arises against a background of long-standing rate inadequacy in both the voluntary market for New Jersey automobile insurance and the residual market (served formerly by the JUA and now by the MTF). That rate inadequacy has been deliberately produced, in large measure, by legislative and regulatory decisions: (1)

to defer payment of the full costs of the automobile insurance system; (2) to shift those costs from the regular ratemaking process by use of subsidies since eliminated by FAIRA; (3) to shift costs from higher loss areas of the State to lower loss areas; and (4) to impose taxes and assessments to cover past deficits while denying any prompt rate adjustment to cover those taxes and assessments. Regulatory efforts to shield the voters from the full costs of the automobile insurance system have also played a part.

Voluntary Market Rate Inadequacy

New Jersey has very expensive automobile insurance because it has a high accident rate, high medical and repair costs, and an automobile insurance system that provides very generous benefits. (ALa 54a-55a) New Jersey also stringently regulates insurance rates, requiring the Commissioner's approval for any increase. *N.J.S.A. 17:29A-4, -14.*¹ The Insurance Department's own studies show that strict regulation has been used "to avoid paying the actual cost of the State's high accident rate and unbalanced no-fault system" and has thereby rendered the system unprofitable for private insurers. (ALa 56a, 47a)

¹ Since 1944, the New Jersey insurance statutes have directed that rates be made "that are not unreasonably high or inadequate for the safety and soundness of the insurer, and which do not unfairly discriminate between risks in this State involving essentially the same hazards and expense elements." *N.J.S.A. 17:29A-4.*

FAIRA has added to the costs of private insurers by imposing taxes and assessments to be used to defray JUA deficits whose origin is discussed below. The substantive terms of FAIRA forbade any recovery of those taxes and assessments from policyholders, though this Court has now held that FAIRA's preamble permits some recovery through rate filings. *State Farm Mutual Automobile Insurance Co. v. Fortunato*, 124 N.J. 32, 590 A.2d 191 (1991).

In August, 1990, shortly after the possibility of such relief was suggested by the Commissioner, Allstate sought a rate increase for this purpose. Only by obtaining a writ from the Superior Court was Allstate able to obtain referral of that application for hearing. *Allstate Insurance Co. v. Fortunato*, 248 N.J. Super. 153, 590 A.2d 690 (App. Div. 1991). No hearing has yet begun. However, even without consideration of Allstate's claimed need for rate relief, it has been required to pay the taxes and assessments for which recovery is sought. Unless its prior rates were grossly excessive, this would have rendered its current rates inadequate for even its existing business.²

² Affidavits show that, based on rate levels at the time of the Depopulation Order, Allstate projected an annual operating loss of \$111 million, of which \$20 million would be attributable to depopulation business. (ALa 43a-45a) In addition to the August, 1990 rate filing seeking recovery of the FAIRA taxes and assessments, Allstate made a filing in October, 1990 seeking an adjustment for its other rate needs. Hearings on that filing began in February, 1991 and it will yet be months before there is a decision.

Since Allstate filed its initial applications for rate increases, events have demonstrated that even larger increases would be

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Even once rate adjustments can be provided for the FAIRA taxes and assessments, FAIRA's restrictions on recovery will require that rates be held to the minimum level consistent with constitutional guarantees on a fair return. *State Farm Mutual Automobile Insurance Co. v. Fortunato*, *supra*, 124 N.J. at 60-62, 590 A.2d at 205-07. Accordingly, voluntary market business can provide no excess profits which could be used to cover rate deficiencies on depopulation assignments.

Moreover, current or past rate inadequacies may not be compensated by granting higher-than-normal rates in the future. *In Re Elizabethtown Water Co.*, 107 N.J. 440, 449-51, 527 A.2d 354, 359-60 (1987); *In re Industrial Sand Rates*, 66 N.J. 12, 23, 327 A.2d 427, 433 (1974). Only the *prospective* costs of the insurance to be provided may be considered in setting rates. Thus, unless current rates are made adequate, an insurer may suffer irrecoverable losses.

The JUA and Creation of the Residual Market Rate Inadequacy

In light of the high costs of no-fault insurance and the difficulty of obtaining rates which would cover those costs, many drivers who would otherwise have been attractive customers were unable to procure insurance in

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necessary just to cover the costs of writing the insurance Allstate is required to write. Accordingly, and in light of the protracted period necessary for rate proceedings, Allstate sought interim rate relief, subject to refund if later found excessive. The Commissioner has never acted on this request.

the voluntary market. To eliminate this obstacle to voluntary writing, the JUA was created.

All New Jersey automobile insurers were required to be members of the JUA. Some insurers were to act as JUA servicing carriers – to issue policies, collect premiums and handle claims. However, neither members nor servicing carriers were to have any liability under JUA policies. *N.J.S.A. 17:30E-7(b), -7(c), -8(a)*.

The Legislature contemplated that the rates permitted on JUA policies would be similar to those charged in the voluntary market, and, so, would not suffice to pay the losses and expenses of those policies. *N.J.S.A. 17:30E-13*.³ Thus, it provided the JUA with additional sources of revenue.

One such source was "policy constants" originally prescribed by the Commissioner to subsidize the former assigned risk plan. These were fixed sums included in all insurance premiums, which private insurers used to partially defray their losses on assigned risk policies. Policy constants were continued under the JUA Act and were required to be remitted to the JUA by the insurers collecting them. *N.J.S.A. 17:30E-8(a); 17:29A-35*. Additionally, the Commissioner was empowered to impose a residual market equalization charge ("RMEC") to be collected by insurers on every insured vehicle and remitted to the JUA. The RMEC was to be set, in light of the other

³ A subsequent Insurance Department study has noted that JUA insureds with clean driving records have accident frequencies 35% higher, on average, than similar insureds in the voluntary market. (ALa 63a)

resources available, to allow the JUA to operate on a no-profit, no-loss basis. *N.J.S.A. 17:30E-3(o), 8(b)*.

By November 8, 1984, less than two years after the JUA was created, the JUA Board – relying on outside consultant actuaries – recognized the JUA was operating at a loss and needed a RMEC to meet its statutory mandate to balance its books. The Board projected a \$200 million deficit for 1984, and, if no RMEC were charged, a nearly \$2 billion deficit for 1990. Rather than approve a RMEC, however, the Commissioner mandated that the JUA adopt a cash-flow method of accounting, paying claims arising out of old policies with premiums received under new policies *without* setting aside the reserves necessary to meet the obligations arising under the policies whose premiums were thus diverted. JUA Plan, Operating Principles, Part I, § 7 (May 24, 1985). RMEC's were later imposed when the JUA's cash-flow needs made this absolutely essential.

Adoption of cash-flow funding for the JUA made an eventual financial disaster virtually inevitable. The JUA was denied revenues adequate to fund the reserves necessary to pay for losses already incurred, thereby creating a deficit in the assets necessary to pay existing claims. The JUA's rates were so severely inadequate that, even with a subsidy from RMEC's and policy constants (totaling roughly \$700 million in 1989 alone), the JUA incurred a deficit of over \$3 billion.

Creation of the MTF and Deepening of the Residual Market Rate Inadequacy

FAIRA abolished the JUA and made certain provisions for funding its accumulated deficit. The JUA was

forbidden to issue or renew any policy after September 30, 1990, so its last policies would expire by September 30, 1991. FAIRA § 16. Significantly, neither RMEC's nor policy constants were to be imposed on or after April 1, 1991. FAIRA § 17.

In light of the JUA's cessation of all writing on September 30, 1990, the MTF was created to arrange for the issuance and renewal of policies from October 1, 1990 through September 30, 1992. FAIRA § 88(a)-(c). The MTF was initially to charge the JUA rates in effect on September 30, 1990. FAIRA § 88(c)(2). The losses suffered by the MTF (or, hypothetically, its profits) were to be shared among the insurers doing business in the voluntary market. FAIRA § 88(a).

The JUA's rates became those of the MTF, *but the MTF is not entitled to either RMEC's or policy constants*. FAIRA § 17. Those subsidies amounted to over 30% of the JUA's inadequate revenues in 1989. Their elimination deepened the JUA/MTF rate inadequacy.

In November, 1990, the MTF obtained two independent actuarial studies indicating that its rates must increase an average of roughly 60% to cover the costs of insuring its current population. The MTF, which is operated by the Insurance Department, sought a rate increase of only 28%. And, on May 10, 1991, the Commissioner entered an order allowing only an 18.6% increase, though virtually conceding that at least a 47.4% increase was indicated by the record before him. Indeed, the 18.6% increase would not even replace the lost JUA subsidies, let alone cover the JUA's rate inadequacy.

Thus, the MTF rates too are wholly inadequate. Accordingly, the remainder of the costs (amounting to hundreds of millions of dollars) of insuring the MTF population will be imposed on Allstate and other private insurers, which are statutorily obligated to absorb the MTF's losses. FAIRA § 88.

Impact of Rate Inadequacy on the Depopulation Order

Policies issued pursuant to the Depopulation Order must be written at Allstate's own voluntary market rates or those of the MTF. However, even were Allstate's voluntary-market rates adequate (which they are not), they would not suffice for JUA/MTF insureds, whose accident frequency is on average substantially higher than comparable voluntary-market insureds. Even the MTF rates, which are generally higher than Allstate's voluntary-market rates, are inadequate.⁴

Absent a rate increase, the record below demonstrated that Allstate would suffer an insurance operating loss for policies written in 1991 of 35% of the premiums earned, an amount estimated at \$111,000,000. Of this loss, approximately \$20,000,000 would be produced by compliance with the Depopulation Order. (ALa 43a-45a)⁵

⁴ This point is underscored by the fact that, as explained *infra*, Allstate is not to be assigned merely a representative share of the JUA/MTF business. It is to be given business selected from the most severely underpriced of the JUA's territories. That nearly triples the expected loss.

⁵ Indeed, even were one to consider all of Allstate's New Jersey insurance business, rather than just its automobile insurance business, Allstate anticipates a substantial operating loss for 1991 absent automobile insurance rate increases. (ALa 44a)

Allstate sought a stay of the Depopulation Order, and then appealed. Allstate's appeal was based on the foregoing showing that neither its own or the MTF's rates are adequate for the risks to be assigned, and that Allstate's own rates are inadequate for the business it already writes – let alone for the higher losses of the business which the Depopulation Order would compel it to write.⁶ Despite Allstate's showing that it would suffer massive losses if compelled to accept depopulation assignments at existing rates, neither the Commissioner nor the Appellate Division found or purported to find those rates adequate. However, neither protected Allstate from the resulting risk of irrecoverable loss.

Disproportionate Assignments by Territory

Insurance rates vary among different locations. In setting rates for individual insureds, insurers utilize many factors which have been found predictive of the differing levels of risk presented by those insureds. Among the most important of these predictive factors is the territory in which a vehicle is located, which reflects population density, traffic conditions, repair costs and other factors which determine the frequency of accidents and the cost levels associated with them.

⁶ Allstate cannot avoid these losses by ceasing to do business in New Jersey, for FAIRA and the Commissioner have forbidden such cessation without more than five years notice and assumption of numerous heavy burdens in the interim. See *In re "Plan of Orderly Withdrawal" of Twin City Fire Ins. Co.*, Docket No. A-114-90T5 (N.J. App. Div. June 11, 1991). Thus, Allstate has been conscripted to remain in New Jersey.

In 1983, the Legislature altered the ratemaking standard by artificially "capping" the differentials in rates to be charged various classes of insureds. *N.J.S.A. 17:29A-36*. In particular, the base rate for a coverage in any given rating territory, exclusive of driving record surcharges and discounts, could not exceed 1.35 times the filer's statewide average base rate for that coverage. *N.J.S.A. 17:29A-36(c)*.

Artificial capping of rate differentials, when actuarial data shows cost differentials exceeding the "caps," requires that some insureds be charged prices which do not reflect the full cost of the insurance provided. This results in creation of a class of underpriced customers, whom no insurer will voluntarily insure, thereby constricting availability of insurance in the voluntary market.

The Depopulation Order computes assignment percentages by territory. Exposures are first assigned from the territory with the smallest percentage of vehicles insured by private insurers, until the remaining JUA/MTF percentage in that territory equals that in the territory with the next lowest private market percentage, and so on until all the necessary assignments are made. The territories in which the MTF has the highest market share are those in which rate-capping has made the rates most inadequate. Thus, the Order assigns to Allstate a disproportionate number of the most inadequately rated risks from the rate-capped territories.

QUESTIONS PRESENTED AND
REASONS FOR CERTIFICATION

This case presents a constitutional issue of first impression before this Court. May an insurer be compelled to accept new business at legally prescribed rates when those rates have never been determined to be adequate for that business, and where the insurer shows *prima facie* that those rates are not adequate for that business and that its other business generates no excess profits which could be used to support inadequate returns on the assigned business? If the Commissioner's Order is allowed to stand, the assets of all insurers in New Jersey (and, particularly, Allstate) will be subject to blatant confiscation through assignments to insure an ever-increasing number of risks at rates which can only be expected to produce substantial losses, both now and in the future.

Moreover, if the Commissioner's Order is allowed to stand, Allstate will be required, now and in the future, to accept a disproportionate number of depopulation assignments from the most inadequately rated territories in New Jersey. This will violate the statutory mandate that depopulation occur pursuant to "an equitable apportionment procedure." (See N.J.S.A. 17:30E-14a, whose meaning is also an important question of first impression.)

COMMENTS ON THE APPELLATE
DIVISION'S OPINION

I. THE APPELLATE DECISION IMPROPERLY
IGNORED ALLSTATE'S PRIMA FACIE SHOWING
OF CONFISCATION.

This Court has explicitly recognized the Commissioner's "duty under the [relevant] statute to assure that insurers receive a constitutionally fair rate of return." *State Farm Mutual Automobile Insurance Co. v. Fortunato*, *supra*, 124 N.J. at 54, 590 A.2d at 202.⁷ Yet, permitting the MTF depopulation to proceed under the Commissioner's Order, especially in light of the MTF Rate Order, results, *prima facie*, in confiscation of Allstate's property. The Appellate Division's decision fails to apprehend and/or provide any remedy for this apparent confiscation.

As described above, Allstate demonstrated, at least *prima facie*, that the rates it is permitted to charge for the business to be assigned are inadequate even to cover the costs of providing this insurance, let alone to provide a

⁷ The power to regulate a business does not include the "power to compel the doing of [regulated] services without reward." *Troy Hills Village v. Township Council*, 68 N.J. 604, 620, 350 A.2d 34, 42 (1975). Nor may such a business be compelled to subsidize the needs of its customers. *Id.* This means that regulated rates must be sufficient not only to cover costs and expenses, but also to yield a profit "sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital." *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944) (citations omitted).

fair return. Nor can the loss imposed by the Depopulation Order be supported by profits from Allstate's voluntary automobile insurance business, for Allstate is experiencing massive operating losses due to FAIRA and the Commissioner's refusal to approve adequate rate increases. Finally, any profits Allstate might hope to make in other New Jersey insurance lines will be completely overwhelmed by its automobile insurance losses, thus producing a large aggregate operating loss on all New Jersey insurance operations of Allstate and its affiliates. By any standard, Allstate has made a *prima facie* showing that the Order has confiscatory impact.

If Allstate is forced to issue policies pursuant to an inadequate rate structure, it will suffer irreparable harm. To begin with, once a policy is issued at an inadequate rate, Allstate is powerless to alter that rate for the duration of the policy. And, as previously explained, Allstate may not recoup any such deficiency in today's rates by attempting to charge higher rates at some time in the future.

The Appellate Division was aware of the Commissioner's MTF rate decision, but determined that it could not "evaluate the impact of his decision on these parties." (Decision, p. 25 n. 8) It thus concluded that depopulation should proceed with the newly enhanced MTF rates - a situation it felt "creates a better situation than was predicted for the insurers at the time of their briefs and oral arguments," although even the Appellate Division recognized that this was perhaps not a situation that is "better enough" (*i.e.*, that it still might not provide adequate rates). (*Id.*, p. 26)

Allstate respectfully submits that, even on the record before the Appellate Division at the time this matter was briefed and argued, Allstate had made a *prima facie* showing of confiscation mandating relief from the Depopulation Order. That showing took full account of the then-pending request for a 28% rate increase, so the smaller increase actually granted certainly could not eliminate the confiscatory impact shown.⁸

Further, unless the losses suffered because of presently inadequate rates will be compensated at some future time, current confiscation cannot be justified on the basis that it will continue only until determination of a final rate of completion of some other proceeding (*i.e.*, Allstate's voluntary-market rate proceedings). In *Pendergast v. New York Telephone Co.*, 262 U.S. 43 (1923), for example, a telephone company was ordered to reduce its rates pending completion of hearings to set rates. The order was said to be "temporary," but (as in New Jersey) no procedure was available to recoup in the future any

⁸ While noting that even the MTF requested less of a rate increase than necessary to "break even," the Appellate Division dismissed the confiscatory nature of the Depopulation Order because it felt it could not determine whether the MTF's rates are inadequate by definition due to their failure to provide a fair rate of return. (Decision, pp. 25-26) It was unnecessary, however, for the Appellate Division even to delve into the issue of whether Allstate would be earning a sufficient return on the business assigned to it to meet constitutional requirements. That issue would have arisen only were Allstate in a position to earn *some* return on MTF policies. But the MTF rates have been set at a level far below that which the MTF-retained actuaries concluded was necessary even to cover the cost of insuring the assigned business.

deficits that might be incurred while the "temporary" order was in effect.

The Supreme Court sustained a preliminary injunction staying the rate reduction but requiring the company to refund any charges above the level originally ordered which were later found excessive. The Court held that the ostensibly temporary character of the order did not:

[D]eprive the Company of its right to relief at the hands of the court. The orders required the new reduced rates to be put into effect on a given date. They were final legislative acts as to the period during which they should remain in effect pending the final determination; and if the rates prescribed were confiscatory the Company would be deprived of a reasonable return upon its property during such period, without remedy, unless their enforcement should be enjoined. Upon a showing that such reduced rates were confiscatory the Company was entitled to have their enforcement enjoined pending the continuance and completion of the rate-making process.

Id. at 49. *Accord Smith v. Illinois Bell Telephone Co.*, 270 U.S. 587, 591-92 (1926) (company suffering from interim confiscatory rates is not required "to await a decision of the ratemaking tribunal before applying to a federal court for equitable relief").

To be sure, it may not be possible to determine finally what rates are required prior to completion of a full rate proceeding. To deal with that problem, this Court has previously approved a procedure by which a temporary, interim rate increase may be granted, with the proceeds of that increase to be held in escrow pending conclusion

of the rate proceeding, subject to refund (with interest) to whatever extent the interim increase is ultimately found excessive. See, e.g., *In re Industrial Sand Rates*, 66 N.J. 12, 25-26, 327 A.2d 427, 434-35 (1974); *New Jersey State AFL-CIO v. Bryant*, 55 N.J. 171, 176-77, 260 A.2d 225, 227-28 (1969). In this way, the regulated company is protected from irreparable loss of revenue to which it is entitled while ratepayers are protected against any ultimate liability for amounts in excess of those which they are in fact obliged to pay.⁹

Nor is the need for emergency relief the result of any lack of diligence by Allstate. Allstate's first application for a rate increase, relating to taxes and assessments, was sought in August, 1990, promptly after the Commissioner

⁹ Of course, a regulated company is not *routinely* entitled to rate relief prior to completion of a rate proceeding. See, e.g., *In re New Jersey Power & Light Co.*, 15 N.J. 82, 90, 104 A.2d 1, 5 (1954). But this is not a case in which the rates were previously set to provide a fair and reasonable return as to the very business the regulated company would be conducting pending the establishment of new rates. Instead, no fair and reasonable rates were *ever* previously established for the business Allstate would be forced to take – the JUA rates were based on cash-flow underwriting (which Allstate is legally forbidden to conduct and which would inevitably confiscate Allstate's property to satisfy obligations for which no reserves would be provided), and on a gargantuan annual subsidy which will not be available to Allstate. Thus, there is no room for any presumption that existing rates are fair and adequate. Indeed, even the Commissioner's MTF Rate Order does not find that the MTF's current allowable rates (after the 18.6% increase) are adequate. Nor could the Commissioner so find in light of his own and the MTF's actuarial studies, showing the need for a rate increase of at least 47.4% for the MTF to break even.

announced the position that these might be recoverable in some circumstances. Allstate's second filing was made in October, 1990, promptly after it became possible to estimate (inadequately, as subsequent events have shown) the rate levels to be required in light of FAIRA and related developments.

In these circumstances, and in the face of a *prima facie* showing that the Depopulation Order will have a confiscatory impact, the Commissioner may not summarily require compliance by simply pointing to a pending rate proceeding. Before demanding compliance, he must be required either to determine, on a judicially reviewable record, that existing rates are adequate, or to permit interim rates appropriate to the *prima facie* showing until the issue of rate adequacy can be resolved.

Despite the strength of Allstate's evidence with regard to the inadequacy of its voluntary market rates, and despite the Appellate Division's reluctance to consider the impact of the MTF rates, the Appellate Division held that Allstate should be forced to proceed with writing the assigned depopulation business at rates that are insufficient even to cover the costs of providing the subject insurance. (Decision, pp. 24-27) The court dismissed, without discussion, Allstate's request to use interim rates if required to accept assignments while the rate adequacy questions were resolved. (*Id.*)

Yet, the interim rate procedure is the *only* means through which issues such as that presented by the Depopulation Order can be resolved with no permanent and irreparable harm to anyone. In the absence of interim rates, irrecoverable confiscation may occur. By allowing

Allstate to charge interim rates, subject to refund (with interest) to whatever extent the interim increase is ultimately found not to have been justified, the Appellate Division could have protected Allstate from irreparable loss with no corresponding harm to the State or Allstate's insureds.¹⁰

II. THE COMMISSIONER'S DEPOPULATION-BY-TERRITORIES SCHEME IS INHERENTLY INEQUITABLE.

N.J.S.A. 17:30E-14(a) provides that depopulation assignments must proceed "pursuant to an equitable apportionment procedure." Yet, rather than randomly assigning them, the Commissioner retroactively determined to systematically assign depopulation exposures from the New Jersey territories with the most inadequate rates.

The first ground cited by the Appellate Division in support of the Commissioner's conduct is that the Commissioner's agreement not to depopulate the worst

¹⁰ The Appellate Division's decision itself suggests the validity of the interim rate procedure. The court stated that "[w]e are in no position . . . to predict whether . . . untested new business taken on by the insurers from the MTF at untested new MTF premium rates will result in future losses so clear and significant that the insurers are entitled to protection in advance." (Decision, p. 26) If, as the court suggested, it was in "no position" to determine Allstate's confiscation claim pending further development of the record, Allstate should at least have been permitted to protect itself from future losses pending that record development.

drivers blunts the impact of his depopulation-by-territories scheme. (Decision, p. 12) But Allstate never argued that the reason for the inequity of the Commissioner's plan is that more of the worst drivers are located in the subject territories. Rather, Allstate's point was that, by requiring it to accept a disproportionate number of assignments from those territories where rate-capping makes rates the most inadequate, the Commissioner was acting inequitably.

In other words, regardless of the characteristics of the drivers in the relevant territories, rate-capping has made those territories the most inadequately rated in the State. Consequently, whether or not the worst drivers are depopulated, the Commissioner's plan will require Allstate to accept a disproportionate number of the most inadequately rated risks.¹¹

The Appellate Division next posited that it would be unfair to place insurers who met their depopulation quotas on a par with insurers, such as Allstate, who did not meet their quotas. (Decision, pp. 12-13) Yet, the

¹¹ The analysis is similar with respect to the Appellate Division's second point – that Allstate would be able to charge MTF rates, and higher rates to bad drivers at that, so depopulation-by-territories should not be inequitable. (Decision, p. 12) Once again, Allstate is not arguing that the inequity of depopulation-by-territories is that Allstate is forced to insure more bad drivers. *All* drivers in the subject territories, be they bad or good, are inadequately rated because of territorial rate-capping. Thus, the ability to charge higher rates to bad drivers will provide some additional revenue to those insuring bad drivers, wherever they reside, but has no impact on the inequity of the Commissioner's depopulation-by-territories scheme.

insurers that have met their quotas have already received a benefit – they have been able to appropriate the most desirable JUA/MTF risks for themselves. The Commissioner's depopulation-by-territories scheme confers an extra benefit upon these insurers – they henceforth neither have to insure the most underpriced risks remaining in the MTF nor bear a share of the losses those risks remaining in the MTF nor bear a share of the losses those risks impose on that entity.

The Commissioner's scheme thus adds a statutorily unauthorized penalty for insurers failing to meet their quotas) *i.e.*, they must insure a disproportionate number of the most inadequately rated risks). Such a result hardly meets the statutory mandate that depopulation be accomplished "equitably."

Finally, the Appellate Division attempts to justify the Commissioner's plan as being "equitable" to New Jersey insureds. (Decision, p. 13) Under no objective standard, however, does it make any difference whether insureds are covered by the MTF or in the voluntary market. No matter who insures a risk, the coverage provided to that insured will be identical. Moreover, all insurers can charge MTF rates to their depopulation assignments, so those assigned will receive no price discount through being insured with voluntary-market insurers rather than in the MTF.

CONCLUSION

For all the foregoing reasons, petitioner Allstate Insurance Company respectfully requests this Court to grant Allstate's Petition for Certification and to proceed to hear this appeal on the merits.

Respectfully submitted,

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CERTIFICATION

I hereby certify that on July 9, 1991 I caused ten copies of a Petition for Certification to New Jersey Supreme Court on behalf of Allstate Insurance Company ("Allstate") together with nine copies of Allstate's Appellate Division Brief and Appendix to be filed with the Clerk of the New Jersey Supreme Court.

In addition, on July 9, 1991 I caused two copies of the within Petition for Certification to be served by hand

upon Douglas S. Eakeley, Acting Attorney General of New Jersey, Richard J. Hughes Justice Complex, CN 112, Trenton, New Jersey 08625, Susan Stryker, Esq., Hannoch Weisman, 50 West State Street, Trenton, New Jersey 08506 and Roselie Burrows, Esq., McCarter & English, Gateway 4, Newark, New Jersey 07102.

Furthermore, the within Petition for Certification presents a substantial question and is filed in good faith and not for purpose of delay. I am aware that if any of the foregoing statements made by me are willfully false, I am subject to punishment.

/s/ Thomas E. Hastings
Thomas E. Hastings

[Appendix Omitted]

APPENDIX 5

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Attorneys for Allstate Insurance Company

IN THE MATTER OF)	SUPREME COURT OF
THE ASSIGNMENT OF	)	NEW JERSEY DOCKET
EXPOSURES TO THE	)	NO.
AETNA CASUALTY	)	SUPERIOR COURT OF
AND SURETY	)	NEW JERSEY APPELLATE
COMPANY, ALLSTATE	)	DIVISION DOCKET NO.
INSURANCE	)	A-2628-90T5F,
COMPANY AND	)	A-2631-90T5F,
COLONIAL PENN	)	A-2783-90T5F
INSURANCE	)	(Consolidated)
COMPANY)	
	)	NOTICE OF APPEAL
)	
	)	On Appeal From:
	)	Final Judgment of the
	)	Appellate Division
)	
	)	Sat Below:
	)	Judges Long,
	)	Cohen and Stern, J.A.D.

TO: THE HONORABLE JUDGES OF THE
SUPREME COURT OF NEW JERSEY

HON. VIRGINIA LONG, J.A.D.
Superior Court of New Jersey
Appellate Division
Hughes Justice Complex

CN-969
Trenton, New Jersey 08625

HON. RICHARD S. COHEN, J.A.D.
Superior Court of New Jersey
Appellate Division
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HON. EDWIN H. STERN, J.A.D.
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PLEASE TAKE NOTICE that, pursuant to Rule 2:2-1(a)(2), Allstate Insurance Company ("Allstate") appeals to the Supreme Court of New Jersey, from a final judgment of the Superior Court of New Jersey, Appellate Division, entered on May 20, 1991, affirming an Order of the Commissioner of Insurance, dated January 24, 1991 (the "Depopulation Order") for the following reasons:

- (1) the Appellate Division decision sustaining the Depopulation Order compels Allstate to accept assigned new business at rates which are inadequate for that business and which, therefore, result in an unconstitutional confiscation of Allstate's property; and
- (2) the Depopulation Order upheld by the Appellate Division disproportionately assigns depopulation business to Allstate from the most inadequately rated territories in New Jersey, thereby violating the statutory mandate that depopulation occur pursuant to "an equitable apportionment procedure," N.J.S.A. 17:30E-14a, and further resulting in an unconstitutional confiscation of Allstate's property.

A copy of the decision appealed from is attached hereto as Exhibit A, and a copy of the Depopulation Order at issue is attached hereto as Exhibit B.

This matter is not entitled to a hearing preference pursuant to Rule 1:2-5.

Dated: Princeton, NJ
July 12, 1991

SMITH, STRATTON, WISE, HEHER &
BRENNAN

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[Exhibits Omitted]

APPENDIX 6

CONSTITUTIONAL PROVISIONS INVOLVED

United States Constitution, Amendment V:

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a grand jury, except in cases arising in the land or naval forces, or in the militia, when in actual service in time of war or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty or property, without due process of law; nor shall private property be taken for public use without just compensation.

United States Constitution, Amendment XIV, Section 1:

All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

APPENDIX 7

STATUTORY AND REGULATORY
PROVISIONS INVOLVED

The Fair Automobile Insurance Reform Act of 1990,
L. 1990, c.8 ("FAIRA"):

FAIRA § 3

3. Section 3 of P.L.1972, c.70 (C.39:6A-3) is amended to read as follows:

3. Compulsory automobile insurance coverage; limits. Every owner or registered owner of an automobile registered or principally garaged in this State shall maintain automobile liability insurance coverage, under provisions approved by the Commissioner of Insurance, insuring against loss resulting from liability imposed by law for bodily injury, death and property damage sustained by any person arising out of the ownership, maintenance, operation or use of an automobile wherein such coverage shall be at least in:

a. an amount or limit of \$15,000.00, exclusive of interest and costs, on account of injury to, or death of, one person, in any one accident; and

b. an amount or limit, subject to such limit for any one person so injured or killed, of \$30,000.00, exclusive of interest and costs, on account of injury to or death of, more than one person, in any one accident; and

c. an amount or limit of \$5,000.00, exclusive of interest and costs, for damage to property in any one accident.

No licensed insurance carrier shall refuse to renew the required coverage stipulated by this act of an eligible person as defined in section 25 of P.L.____, c.____ (C.____(now pending in the legislature as this bill) except in accordance

with the provisions of section 26 of P.L.1988, c.119 (C.17:29C-7.1) or with the consent of the Commissioner of Insurance.

FAIRA § 16

16. Section 19 of P.L.1983, c.65 (C.17:30E-7) is amended to read as follows:

19. Pursuant to the plan of operation, the association shall have the power and duty to:

* * *

b. Sue or be sued in the name of the association, including taking any legal actions necessary or proper for recovery of any assessments for, on behalf of, or against members. A judgment against the association shall not create any direct liability against the servicing carrier, board of directors or the individual members, or the individual participating members of the association;

c. Indemnify its directors and employees for any and all claims, suits, costs of investigations, costs of defense, settlements or judgments against them on account of an act or omission in the scope of a director's duties or employee's employment. The association shall refuse to indemnify if it determines that the act of failure to act was because of actual fraud, willful misconduct or actual malice;

* * *

e. Arrange for the issuance of automobile insurance to any qualified applicant through servicing carriers.

Each servicing carrier shall issue policies in the name of the servicing carrier, on behalf of the association, to the extent the plan of operation provides. Servicing carriers, as agents of the association, shall have no individual liability for claims or policies written by the association. *However, notwithstanding the above, or any other provision of law to the contrary, the association shall not arrange for the issuance or renewal of any automobile insurance policy, either through a servicing carrier or on its own behalf, on or after October 1, 1990;*

* * *

r. Develop methods and standards for the establishment of adequate, actuarially sound reserves for unpaid losses and loss adjustment expenses, including provision for incurred but not reported losses.

FAIRA § 17

17:33B-6. Residual market equalization charges or flat charges

Notwithstanding any of the provisions of sections 13 to 34 of P.L.1983, c. 65 (C.17:30E-1 et seq.), section 1 of P.L.1984, c. 1 (C.17:29A-37.1) or any other law, to the contrary, no residual market equalization charges, or flat charges (also referred to as flat capitation fees or policy constants) of any kind, other than the flattened tax and expense fees implemented pursuant to section 8 of P.L.1983, c. 65 (C.17:29A-37), shall continue to be imposed or be imposed on or after April 1, 1991 on a per car or per coverage basis on automobile insurance policies or on policies insuring motor vehicles other than automobiles.

FAIRA §18

18. Section 1 of P.L.1984, c.1 (C.17:29A-37.1) is amended to read as follows:

1. a. All flat charges (also referred to as flat capitation fees or policy constants, but not including premiums for uninsured motorist or towing coverage, or flattened tax and expense fees implemented pursuant to section 8 of P.L.1983, c.65 (C.17:29A-37)), authorized by the Commissioner of Insurance for use by all filers, as defined in section 1 of P.L.1944, c.27 (C.17:29A-1), writing private passenger automobile insurance in the voluntary and residual markets, which are [collected] *imposed* on a per car and per coverage basis on automobile insurance policies issued or renewed in the voluntary or residual market [,with an effective date of January 1, 1984 or thereafter,] *prior to April 1, 1991* shall be paid to the New Jersey Automobile Full Insurance Underwriting Association for use for association purposes. All moneys collected from the flat charges shall be certified to by the filers, including servicing carriers of the association, and transferred, net of a pro rata portion of any producer commissions and all premium taxes payable thereon, to the association in accordance with the provisions of this subsection and the association's plan of operation. No other expenses shall be payable to or deductible from the flat charges transferable to the association.

Flat charges collected under this subsection shall be transferred to the association within 10 days of the close of the month of receipt by the insurer or servicing carrier. In the case of policy premiums paid in accordance with a payment plan or other installment basis, the insurer shall, within 10 days of the close of the month of receipt of

payment, transfer to the association a proportionate share of the total flat charges on the policy, based on the payment schedule or amount of payment received.

b. [Flat charges collected on any automobile insurance policy written in the voluntary or residual market with an effective date prior to January 1, 1984, the policy term of which, however, extends into 1984, shall be retained by the insurer or filer; except that if a policy subject to this subsection has been canceled for reasons other than nonpayment of premium, the insurer or filer shall retain only that portion of the flat charges earned on the policy up to the date of cancellation and shall return any unearned remainder to the policyholder in the same manner as other unearned premiums.]

Flat charges shall not be deemed to include any moneys collected from any residual market equalization charge levied pursuant to section 20 of P.L.1983, c.65 (C.17:30E-8).

Flat charges collected in accordance with subsection a. of this section shall be considered in determining taxable premiums in accordance with P.L.1945, c.132 (C.54:18A-1 et seq.), but shall not be considered in determining excess profits in accordance with section [2 of P.L.1983, c.357 (C.17:29A-5.3)] *section 3 of P.L.1988, c.118 (C.17:29A-5.8).*

c. The flat charges authorized by the Commissioner of Insurance for private passenger automobile insurance in the voluntary and residual markets may be imposed *prior to April 1, 1991* upon all insured motor vehicles other than private passenger automobiles, including motor vehicles insured by the automobile insurance plan established pursuant to P.L.1970, c.215 (C.17:29D-1), and

motor vehicles of a type, as is determined by the Commissioner of Insurance, which are registered with the Division of Motor Vehicles as self-insured vehicles pursuant to section 30 of P.L.1952, c.173 (C.39:6-52), in accordance with rules and regulations established by the commissioner. In the case of motor vehicles other than private passenger automobiles which are insured by an insurer in the voluntary market or in any insurance plan established pursuant to P.L.1970, c.215 (C.17:29D-1), the insurer shall forward the flat charge, net of a pro rata portion of the producer's commission, to the New Jersey Automobile Full Insurance Underwriting Association. In the case of a self-insurer required to pay a flat charge, the self-insurer shall forward the full amount of the flat charge to the association. The Division of Motor Vehicles shall not issue a certificate of self-insurance unless the association has certified that the flat charge has been paid. Failure to pay the flat charge shall constitute a reasonable ground for cancellation of a certificate of self-insurance pursuant to section 30 of P.L.1952, c.173 (C.39:6-52). Any self-insurer which fails to pay the flat charge to the association for any self-insured vehicle shall be liable to pay a fine in the amount of \$100.00 per vehicle for the first offense and \$200.00 for the second and each subsequent offense.

Notwithstanding any other provision of this section, flat charges shall be imposed on such motor vehicles *prior to April 1, 1991* as are determined by the Commissioner of Insurance, which vehicles have been registered with the Division of Motor Vehicles in accordance with Title 39 of the Revised Statutes as commercial motor vehicles and have been issued commercial license plates or farmers'

license plates, and on motor vehicles, of a type determined by the Commissioner of Insurance, which are registered with the Division of Motor Vehicles as self-insured vehicles pursuant to section 30 of P.L.1952, c.173 (C.39:6-52).

FAIRA § 20

20. Section 26 of P.L.1983, c.65 (C.17:30E-14) is amended to read as follows:

26. a. Within 45 days of the effective date of this 1988 amendatory and supplementary act, the commissioner shall, in the plan of operation, establish procedures to govern the voluntary writing of applicants and association insureds without the utilization of the association. These procedures shall include criteria identifying drivers who should be eligible for coverage in the voluntary market. Applicants and association insureds meeting these criteria shall be subject to assignment by the association to member companies, pursuant to an equitable apportionment procedure established in the plan of operation. The procedure shall give due consideration to the increase or decrease in the volume of private passenger automobile non-fleet exposures voluntarily written by member companies in this State since January 1, 1984.

b. (1) Pursuant to the procedures established in the plan of operation under subsection a. of this section, the commissioner shall establish a voluntary market quota, which shall not be less than 60% of the aggregate number of private passenger automobile non-fleet exposures written in the total private passenger automobile insurance market in this State on the effective date of this

1988 amendatory and supplementary act. The quota shall prescribe the number of voluntary market exposures which shall be written by member companies during the 12 month period beginning 60 days after the effective date of this 1988 amendatory and supplementary act.

(2) [At the end of the first 12 month period following the effective date of this 1988 amendatory and supplementary act] *Within 30 days of the effective date of P.L.____, c. (C.____)(now pending in the Legislature as this bill)*, the commissioner shall prescribe a second quota, which shall take effect [no later than 60 days following the end of that period] *immediately upon adoption by the commissioner* and which shall not be less than [70%]68% of the aggregate number of private passenger automobile non-fleet exposures written in the total private passenger automobile insurance market in this State [at the end of the first 12 month period following the effective date of this 1988 amendatory and supplementary act] *on or before October 1, 1990*. The quota shall prescribe the number of voluntary market exposures which shall be written by member companies during the [12 month] period described in this paragraph.

(3) [At the end of the second 12 month period following the effective date of this 1988 amendatory and supplementary act, the commissioner shall prescribe a third quota, which shall take effect no later than 60 days following the end of that period and which shall not be less than 75% of the aggregate number of private passenger automobile non-fleet exposures written in the total private passenger automobile insurance market in this State at the end of the second 12 month period following the effective date of this 1988 amendatory and supplementary act. The quota shall prescribe the number of

voluntary market exposures which shall be written by member companies during the 12 month period described in this paragraph.](Deleted by amendment, P.L. ___, c. ___.)*(now pending before the Legislature as this bill)*

(4) [No later than 60 days following the end of the third 12 month period following the effective date of this 1988 amendatory and supplementary act, the commissioner shall prescribe such a quota that will result, at the end of the fourth 12 month period following the effective date of this 1988 amendatory and supplementary act, in the volume of exposures written in the voluntary market equaling no less than 80% of the aggregate number of private passenger automobile non-fleet exposures being written in the total private passenger automobile insurance market in this State, or such volume of exposures in excess of 80% that the commissioner determines should be considered eligible for coverage in the voluntary market. The quota shall prescribe the number of voluntary market exposures which shall be written by member companies during the 12 month period described in this paragraph. After the period established in this paragraph, the association shall not write any risk for a period longer than three years, unless, at the end of that time, the insured has presented evidence that he has been rejected by at least two insurers in the voluntary market.] (Deleted by amendment, P.L. ___, c. ___.)*(now pending before the Legislature as this bill)*

c. In the event that any of the quotas established by the commissioner pursuant to subsection b. of this section have not been met by the end of any [12 month] *applicable* period, the commissioners shall direct the association to assign the balance of the exposures needed to meet the

applicable quota to member companies in a manner consistent with the apportionment procedure established pursuant to subsection a. of this section. A member company which [exceeds] *exceeded* its apportionment share for [any] *the* 12 month period *prescribed pursuant to paragraph (1) of subsection b. of this section* shall receive credit for the excess against the [following year's obligation] *quota imposed pursuant to paragraph (2) of subsection a. of this section.*

d. [If, at any time after the period established in paragraph (4) of subsection b. of this section, the volume of exposures written in the voluntary market equals less than 80% of the aggregate number of private passenger automobile non-fleet exposures being written in the total private passenger automobile insurance market in this State or such volume of exposures in excess of 80% that the commissioner determines should be eligible for coverage in the voluntary market, the commissioner shall direct the association to assign eligible applicants and association insureds to member companies on an equitable basis.] [*Deleted by amendment, P.L. ___, c. ___.*](*now pending before the Legislature as this bill*)

e. For the purposes of this section, any exposure written in the voluntary market by an affiliate of the insurer to which an apportioned share has been assigned shall be credited against that share.

f. The total number of exposures written in the voluntary market, net of exposures cancelled or non-renewed, by a member company at the end of the applicable period shall be utilized in determining

whether the member company has written its apportionment share in the voluntary market for purposes of complying with any quotas established by the commissioner pursuant to this section.

g. The commissioner may excuse a member company from meeting any of its obligations under this section that he determines would result in the member company being in an unsafe or unsound condition.

h. Any member company that does not write its apportionment share of any quota established by the commissioner pursuant to subsection b. or c. of this section within the applicable time period shall be precluded from nonrenewing automobile insurance policies pursuant to section 26 of [this 1988 amendatory and supplementary act] *P.L.1988, c.119 (C.17:29C-7.1)* during the immediately following 12 month period.

i. In addition to the requirements of subsection a. of this section, the procedures governing the increase in voluntary market volume shall:

(1) establish guidelines and criteria for determining whether a person is a qualified applicant as defined in section 15 of *P.L.1983, c.65 (C.17:30E-3)*, and procedures for the issuance of automobile insurance through the voluntary market to persons found not to be qualified applicants for association coverage, and for the referral of persons determined not to be eligible for association coverage to alternative residual market mechanisms;

(2) include provisions ensuring that servicing carriers do not obtain any unfair advantage over other member companies in the selection of qualified applicants and association insureds to be written as voluntary business;

(3) neither prohibit nor require member companies to write association business through association producers of record, provided, however, that where a member company elects not to service such business through the association producer of record, the procedures shall address the manner in which the association shall transfer the business to the member company, and shall establish reasonable compensation in an amount sufficient to offset the actual expenses incurred by the association producer in conjunction with the transfer which shall be paid by the association upon transfer of the business to the member company; and

(4) provide for financial disincentives to applicants who, without good cause, reapply for coverage in the association after being placed in the voluntary market.

FAIRA § 23

17:33B-5. New Jersey automobile insurance guaranty fund

a. There is hereby created within the General Treasury a special nonlapsing fund to be known as the New Jersey Automobile Insurance Guaranty Fund. The State Treasurer shall credit to the fund, in addition to any sums appropriated thereto, all monies designated in subsection b. of this section and collected pursuant to this act on and

after the effective date of this 1990 amendatory and supplementary act. Monies credited to the New Jersey Automobile Insurance Guaranty Fund may be invested in the same manner as assets of the General Fund and any investment earnings on the fund shall accrue to the fund and shall be available subject to the same terms and conditions as other monies in the fund. The State Treasurer may determine the amount of earnings to be credited to the New Jersey Automobile Insurance Guaranty Fund to reflect the average rate of return on the State of New Jersey Cash Management Fund.

b. Monies from the following sources shall be credited by the State Treasurer to the New Jersey Automobile Insurance Guaranty Fund: the revenues attributable to the surtax imposed under section 76 of this 1990 amendatory and supplementary act (C.17:33B-49); the revenues attributable to the tax imposed on premiums earned by the New Jersey Automobile Full Insurance Underwriting Association pursuant to section 34 of P.L.1983, c.65 (C.17:30E-22); that percentage of surcharges collected by the Division of Motor Vehicles on or after October 1, 1991, pursuant to subsection b. of section 6 of P.L.1983, c.65 (C.17:29A-35); monies collected by the Division of Motor Vehicles on or after October 1, 1991, pursuant to section 68 of this 1990 amendatory and supplementary act (C.17:33B-63); monies collected by the State Board of Medical Examiners pursuant to section 63 of this 1990 amendatory and supplementary act (C.17:33B-58); monies collected by the State Board of Chiropractic Examiners pursuant to section 64 of this 1990 amendatory and supplementary act (C.17:33B-59); monies collected by the State Board of Physical Therapy pursuant to section 65 of

this 1990 amendatory and supplementary act (C.17:33B-60); monies collected by the Division of Motor Vehicles pursuant to section 66 of this 1990 amendatory and supplementary act (C.17:33B-61); monies collected by the State Treasurer pursuant to section 67 of this 1990 amendatory and supplementary act (C.17:33B-62); loans made to the fund as provided in subsection c. of this section; and such other income as may be deposited with or otherwise made available to the New Jersey Automobile Full Insurance Underwriting Association on or after October 1, 1991, including monies deposited in the New Jersey Automobile Full Insurance Underwriting Association Auxiliary Fund pursuant to section 5 of P.L.1983, c.320 (C.17:33A-5).

c. (1) The fund shall borrow such monies as are made available by the New Jersey Property-Liability Insurance Guaranty Association pursuant to paragraph (10) of subsection a. of section 8 of P.L.1974, c.17 (C.17:30A-8).

(2) The fund may, upon the approval of the Commissioner of Insurance and pursuant to terms and conditions established by him, borrow monies from any other available source.

d. The monies in the New Jersey Automobile Insurance Guaranty Fund, including interest earnings thereon, are specifically dedicated and shall be utilized exclusively for the costs of the purposes of satisfying the financial obligations of the New Jersey Automobile Full Insurance Underwriting Association, as provided in this 1990 amendatory and supplementary act. Those monies are hereby appropriated for those purposes; provided, however, that

those monies shall be disbursed by the State Treasurer as provided in subsection e. of this section.

e. The trustee appointed pursuant to section 21 of this 1990 amendatory and supplementary act shall prepare a written application for any disbursement of monies from the New Jersey Automobile Insurance Guaranty Fund, specifying the amount of the disbursement, the intended expenditures, and the manner in which such expenditures serve the purposes of the trustee's function and this act. The application shall be submitted to the Commissioner of Insurance for approval. Upon approval by the commissioner, the application shall be forwarded to the State Treasurer for approval. Upon approval by the State Treasurer, he shall disburse monies from the New Jersey Automobile insurance Guaranty Fund to the trustee for disbursement as provided in the approved application.

FAIRA § 24

17:33B-22. Automobile insurance coverage for ineligible persons

Those persons who do not qualify as "eligible persons" as defined in section 25 of this 1990 amendatory and supplementary act but who are in good faith entitled to, but are unable to procure automobile insurance coverage, shall be provided automobile insurance

coverage pursuant to the provisions of section 1 of P.L.1970, c.215 (C.17:29D-1)

FAIRA § 25

17:33B-13. Definitions

As used in sections 25 through 33 of this 1990 amendatory and supplementary act:

* * *

"Eligible person" means a person who is an owner or registrant of an automobile registered in this State or who holds a valid New Jersey driver's license to operate an automobile, but does not include any person:

a. Who, during the three-year period immediately preceding application for, or renewal of, an automobile insurance policy has been convicted pursuant to R.S.39:4-50 or section 2 of P.L.1981, c.512 (C.39:4-50.4a), or for an offense of a substantially similar nature committed in another jurisdiction; has been convicted of a crime of the first, second or third degree resulting from the use of a motor vehicle; or has been convicted of theft of a motor vehicle;

b. Whose driver's license to operate an automobile is under suspension or revocation;

c. Who has been convicted, within the five-year period immediately preceding application for or renewal of a policy of automobile insurance, of fraud or intent to

defraud involving an insurance claim or an application for insurance; or who has been successfully denied, within the immediately preceding five years, payment by an insurer of a claim in excess of \$1,000 under an automobile insurance policy, if there was evidence of fraud or intent to defraud involving the automobile insurance claim or application:

d. Whose policy of automobile insurance has been canceled because of nonpayment of premium or financed premium within the immediately preceding two-year period, unless the premium due on a policy for which application has been made is paid in full before issuance or renewal of the policy:

e. Who fails to obtain or maintain membership or qualification for membership in a club, group, or organization, if membership is a uniform requirement of the insurer as a condition of providing insurance, and if the dues or charges, if any, or other conditions for membership or qualifications for membership are applied uniformly throughout this State, are not expressed as a percentage of the insurance premium, and do not vary with respect to the rating classification of the member or potential member except for the purpose of offering a membership fee to family units. Membership fees, if applicable, may vary in accordance with the amount or type of coverage if the purchase of additional coverage, either as to type or amount, is not a condition for reduction of dues or fees;

f. Whose driving record for the three year period immediately preceding application for or renewal of a policy of automobile insurance has an accumulation of

automobile insurance eligibility points as determined under the schedule promulgated by the commissioner pursuant to section 26 of this act; or

g. Who possesses such other risk factors as determined to be relevant by rule or regulation of the commissioner.

FAIRA § 26

17:33B-14. Schedule of automobile insurance eligibility points

The commissioner shall, within 90 days of the effective date of this act, promulgate a schedule of automobile insurance eligibility points by rule or regulation adopted pursuant to the "Administrative Procedure Act," P.L.1968, c.410 (C.52:14B-1 et seq.). The schedule shall assess a point valuation to driving experience related violations and shall include assessments for violations of lawful speed limits within such increments as determined by the commissioner, other moving violations, and at-fault accidents. For the purposes of this section, an "at-fault accident" means an at-fault accident which results in payment by insurer of at least a \$500 claim.

FAIRA § 27(b)

17:33B-15. Coverage for eligible persons: refusal to insure or renew, or limitation of coverage, prohibited

* * *

b. No insurer shall refuse to insure, refuse to renew, or limit coverage available for automobile insurance to an eligible person who meets its underwriting rules as filed with and approved by the commissioner in accordance with the provisions of section 7 of P.L.1988, c.156 (C.17:29A-46). The commissioner may suspend, revoke or otherwise terminate the certificate of authority to transact automobile insurance business in this State of any insurer who violates the provisions of this section.

FAIRA § 37

37. Section 6 of P.L.1988, c.156 (C.17:29A-45) is amended to read as follows:

6. a. Notwithstanding the provisions of P.L. 1944, c.27 (C.17:29A-1 et seq.) to the contrary, every insurer transacting or proposing to transact private passenger automobile insurance may file rating plans in the voluntary market for standard risks, or non-standard risks, or both. [A rating plan may include a good driver discount plan.] Within 30 days following the effective date of this 1988 amendatory and supplementary act, every insurer writing private passenger automobile insurance in this

State which intends to write coverage in the voluntary market using more than one rate level shall file with the commissioner the rates and underwriting rules which are applicable to each rate level.

b. An insurer which intends to use more than one rating plan and which has a rating plan on file as of the effective date of this 1988 amendatory and supplementary act, may make an initial filing for the additional rating plan in which the modification of the plan on file is expressed as a percentage increase or decrease of the existing rate level.

c. Notwithstanding any other law to the contrary any rates filed pursuant to subsection b. of this section shall be deemed to be approved if not disapproved by the commissioner within 60 days. Any subsequent modification of any rate level other than that provided for in section 5 of this 1988 amendatory and supplementary act, or any initial rate level which is not expressed as percentage increase or decrease of an existing rate level as provided for in this section, shall be subject to the provisions of P.L.1944, c.27 (C.17:29A-1 et seq.).

d. Any limitation on rates established by the provisions of section 7 of P.L.1983, c.65 (C.17:29A-36) shall apply separately to each rate level established pursuant to subsection a. of this section.

e. Every insurer shall maintain such data for each level as may be required by the commissioner by regulation for the purpose of determining excess profits pursuant to the provisions of P.L.1988, c.118 (C.17:29A-5.6 et seq.).

f. No more than 15 percent of the aggregate number of private passenger automobile non-fleet exposures being written in the total private passenger automobile insurance market in this State shall be provided through the non-standard voluntary market as defined by rule or regulation of the commissioner adopted pursuant to the "Administrative Procedure Act," P.L.1968, c.410 (C.52:14B-1 et seq.). If the commissioner certifies that 15 percent or more of the aggregate number of private passenger automobile non-fleet exposures being written in the total private passenger automobile insurance market in this State are insured in the non-standard voluntary market, no insurer transacting automobile insurance in this State shall refuse to issue or renew an automobile insurance policy in the voluntary market for an eligible person as defined in section 25 of P.L. , c.(C.) (now pending in the Legislature as this bill) until such time that the commissioner certifies that the non-standard market comprises less than 15 percent of the aggregate number of private passenger automobile non-fleet exposures being written in the total private passenger automobile insurance market in this State.

g. Notwithstanding any provision of this or any other section of law to the contrary, no insurer shall file, nor shall the commissioner approve, any rates filed for non-standard risks in the voluntary market in excess of 135 percent of the cost of private passenger automobile insurance in the voluntary market in this State as determined by the commissioner.

h. The commissioner shall monitor and report to the Legislature, on March 1, 1992, and annually thereafter, the number of private passenger automobile non-fleet exposures insured in the standard market on December 31 of the preceding calendar year and the number of such exposures insured in

the non-standard market on December 31 of the preceding calendar year.

FAIRA § 38

38. Section 7 of P.L.1988, c.156 (C.17:29A-46) is amended to read as follows:

7. a. Insurers shall put in writing all underwriting rules applicable to each rate level utilized pursuant to section 6 of this 1988 amendatory and supplementary act. No underwriting rule shall operate in such a manner as to assign a risk to a rating plan on the basis of the territory in which the insured resides. An insurer which knowingly fails to transact automobile insurance consistently with its underwriting rules shall be subject to a fine of not less than \$500.00 for each violation.

b. All underwriting rules applicable to each rate level as provided for in section 6 of this 1988 amendatory and supplementary act shall be filed with the commissioner and shall be subject to his prior approval. All underwriting rules shall be subject to public inspection. Insurers shall apply their underwriting rules uniformly and without exception throughout the State, so that every applicant or insured conforming with the underwriting rules will be insured or renewed, and so that every applicant or insured not conforming with the underwriting rules will be refused insurance or be nonrenewed.

FAIRA § 39

17:33B-25. Refusal to issue or renew policy prohibited

Notwithstanding the provisions of section 27 of this 1990 amendatory and supplementary act, section 2 of P.L.1968, c.158 (C.17:29C-7), section 26 of P.L.1988, c.119 (C.17:29C-7.1) or any other section of law to the contrary, if the plan for automobile insurance established pursuant to section 1 of P.L.1970, c.215, (C.17:29D-1), is not accepting new applications for coverage pursuant to subsection d. of that section, no insurer transacting automobile insurance in this State shall refuse to issue or renew any private passenger automobile insurance policy in this State.

FAIRA § 40

17:33B-32. Factors used in determining rates and premiums

a. Notwithstanding any other provision of law to the contrary, rates and premiums for private passenger automobile insurance shall be determined by the application of the following factors in decreasing order of importance:

(1) The insured's driving safety record, including motor vehicle points as provided in Title 39 of the Revised Statutes, at-fault accidents and convictions pursuant to R.S.39:4-50 or section 2 of P.L.1981, c.512 (C.39:4-50.4a) or offenses of a substantially similar nature committed in another jurisdiction;

- (2) The number of miles the insured drives annually;
- (3) The number of years of driving experience the insured has had;
- (4) The type of private passenger automobile driven; and
- (5) Such other factors as the Commissioner of Insurance may adopt by regulation which have a substantial relationship to the risk of loss. The regulations shall also set forth the respective weight to be given to each factor in determining automobile insurance rates and premiums.

b. Notwithstanding any provision of subsection a. of this section to the contrary, rates and premiums for private passenger automobile insurance shall not be determined, in whole or in part, directly or indirectly, upon the age, sex or marital status of the persons insured.

c. The commissioner shall, no later than January 1, 1992, promulgate a plan providing for the implementation of the provisions of subsections a. and b. of this section which shall take effect no later than one year following the date of promulgation.

FAIRA § 72

17:33B-30. Foreign companies; surrender of certificate; plan for withdrawal

An insurance company of another state or foreign country authorized under chapter 32 of Title 17 of the Revised Statutes to transact insurance business in this State may surrender to the commissioner its certificate of

authority and thereafter cease to transact insurance in this State, or discontinue the writing or renewal of one or more kinds of insurance specified in the certificate of authority, only after the submission of a plan which provides for an orderly withdrawal from the market and a minimization of the impact of the surrender or discontinuance on the public generally and on the company's policyholders in this State. The plan shall be approved by the commissioner before the withdrawal or discontinuance takes effect. In reviewing a plan for withdrawal under this section, the commissioner shall consider, and may require as a condition of approval, whether some or all other certificates of authority issued pursuant to chapter 17 or 32 of Title 17 of the Revised Statutes held by the company or by other companies in the same holding company as the company submitting the plan should be surrendered. The certificate of authority of the company shall be deemed to continue in effect until the provisions of the approved plan have been carried out. The provisions of this section shall apply to any request for withdrawal, surrender or discontinuance filed on or after January 25, 1990.

FAIRA § 74

74. Section 8 of P.L.1974, c.17 (C.17:30A-8) is amended to read as follows:

8 a. The association shall:

* * *

(9) Assess member insurers in amounts necessary to make loans pursuant to paragraph (10) of this subsection. [The] Estimated assessments of each member insurer shall be in the proportion that the net direct written premiums of the member insurer for the calendar year preceding the assessment bears to the net direct written premiums of all member insurers for the calendar year preceding the assessment with actual assessments adjusted in the succeeding year based on the proportion that the insurer's net direct written premiums in the year of assessment bears to the net direct written premiums of all member insurers for that year. [However, the association may, subject to the approval of the commissioner, exempt, abate or defer, in whole or in part the assessment of any member insurer, if the assessment would cause the member insurer's financial statement to reflect amounts of capital or surplus less than the minimum amounts required for a certificate of authority by any jurisdiction in which the member insurer is authorized to transact insurance. In the event an assessment against a member insurer is exempted, abated, or deferred, in whole or in part, because of the limitations set forth in this paragraph, the amount by which such assessment is exempted, abated, or deferred, shall be assessed against the other member insurers in a manner consistent with the basis for assessments set forth in this paragraph.]

(10) Make loans in the amount of \$160 million per calendar year, beginning in calendar year 1990, to the New Jersey Automobile Insurance Guaranty Fund created pursuant to section 23 of P.L. __, c. __ (C. __) (now pending in the Legislature as this bill), except that no

loan shall be made pursuant to this paragraph after December 31, 1997.

* * *

FAIRA § 75

75. Section 16 of P.L.1974, c.17 (C.17:30A-16) is amended to read as follows:

16. a. The commissioner shall adopt rules permitting member insurers to recoup over a reasonable length of time, a sum reasonably calculated to recoup assessments paid by the member insurer [under this act] *pursuant to paragraph (3) of subsection a. of section 8 of P.L.1974, c.17 (C.17:30A-8)* by way of a surcharge on premiums charged for insurance policies to which this act applies [; b. the] . *The* amount of any surcharge shall be determined by the commissioner [; c. the] . *The* commissioner may permit an insurer to omit collection of the surcharge from its insureds when the expense of collecting the surcharge would exceed the amount of the surcharge, provided that nothing in this [section] *subsection* shall relieve the insurer of its obligation to remit the amount of surcharge otherwise collectible.

b. *No member insurer shall impose a surcharge on the premiums of any policy to recoup assessments paid pursuant to paragraph (9) of subsection a. of section 8 of P.L.1974, c.17 (C.17:30A-8).*

FAIRA § 76

17:33B-49. Annual surtax on premiums; payment

a. in addition to the tax on net premiums paid pursuant to section 1 of P.L.1945, c.132 (C.54:18A-1), each taxpayer under that section shall pay to the Director of the Division of Taxation an annual surtax at a rate of 5%, or a rate adjusted pursuant to section 77 of this 1990 amendatory and supplementary act, on all taxable premiums collected in this State, except premiums collected by the New Jersey Automobile Full Insurance Underwriting Association *created pursuant to section 16 of P.L. 1983, c.65 (C.17:30E-4), and premiums collected by the Market Transition Facility created pursuant to section 88 of P.L.1990, c.8 (C.17:33B-11)*, in calendar years 1990, 1991 and 1992 for contracts of automobile insurance, notwithstanding section 6 of P.L.1945, c.132 (C.54:18A-6). The surtax shall be administered pursuant to the provisions of P.L.1945, c.132 (C.54:18A-1 et seq.), except that if any provision of that act is in conflict with a specific provision of this 1990 amendatory and supplementary act, the provision or provisions of this 1990 amendatory and supplementary act shall govern.

b. For the purposes of sections 76 through 78 of this 1990 amendatory and supplementary act:

"Automobile" means a private passenger automobile of a private passenger or station wagon type that is owned or hired, and is neither used as a public or livery conveyance for passengers nor rented to others with a driver; a motor vehicle with a pickup body, a delivery sedan, a van, or a panel truck or a camper type vehicle used for recreational purposes, owned by an individual

or by husband and wife who are residents of the same household, not customarily used in the occupation, profession or business of the insured other than farming or ranching. An automobile owned by a farm family co-partnership or corporation, which is principally garaged on a farm or ranch and otherwise meets the definition contained in this section, shall be considered a private passenger automobile owned by two or more relative resident in the same household; and

"Automobile insurance" means direct insurance against injury or damage, including the legal liability therefor, arising out of the ownership, operation, maintenance or use of an automobile, including, but not limited to, personal injury protection insurance, bodily injury liability insurance, property damage liability insurance, physical damage insurance and uninsured and underinsured motorist insurance.

c. Each taxpayer shall:

(1) on or before the first day of the third month following enactment of this 1990 amendatory and supplementary act make an installment payment of surtax due under subsection a. of this section in an amount equal to one half of the surtax estimated to be due for taxable premiums collected in this State in calendar year 1990 is the surtax rate at the time of the payment was imposed for the entire year; and

(2) on or before the first day of the sixth month following enactment of this 1990 amendatory and supplementary act, make an installment payment of surtax due under subsection a. of this section in an amount equal to one half of the surtax estimated to be due for taxable

premiums collected in this State in calendar year 1990 if the surtax rate at the time of the payment was imposed for the entire year; provided however, that no installment payment shall be due if the payment date of such installment pursuant to this subsection falls on or after February 1, 1991.

In the calculation of the tax due in accordance with subsection a. of this section, a taxpayer shall be entitled to a credit in the amount of the tax paid under this subsection as a partial payment and shall be entitled to the return of any amount so paid which is in excess of the total amount payable in accordance with this section.

d. Failure to pay any installment payment required pursuant to subsection c. of this section shall constitute a deficiency, and there shall be added to the tax for the calendar year interest on the amount of underpayment as provided in the State Tax Uniform Procedure Law, R.S. 54:48-1 et seq., for the period of the underpayment.

The amount of underpayment shall be the excess of the amount of the installment payment which would be required to be paid if the installment payment were equal to 45% of the surtax which would be shown on the return for the year if the surtax rate at the time of the payment were imposed for the entire year, or if no return was filed, 45% of the tax for that year, over the amount, if any, of the installment payment paid on or before the last date prescribed for payment.

For purposes of this subsection, the period of the underpayment shall run from the date the installment payment was required to be paid to the earlier of the date on which the surtax is due pursuant to subsection a. of

this section or, with respect to any portion of the underpayment, the date on which that portion is paid.

For purposes of this subsection, a payment of any installment payment shall be considered a payment of any previous underpayment only to the extent that such payment exceeds the amount of the installment payment determined under this subsection for that installment payment.

e. All revenues collected from the surtax imposed pursuant to this section, less any refunds paid pursuant to subsection d. of section 77 of this 1990 amendatory and supplementary act, shall be credited by the State Treasurer to the New Jersey Automobile Insurance Guaranty Fund, created pursuant to section 23 of this 1990 amendatory and supplementary act.

FAIRA § 77

17:33B-50. Adjustment of rate of surtax; estimate of revenues; refund of excess

a. The Director of the Division of Taxation is hereby authorized to adjust the rate of the surtax imposed pursuant to section 76 of this 1990 amendatory and supplementary act, for any of the calendar years in which the surtax is imposed, as provided in this section.

b. The Director of the Division of Taxation, in consultation with the Commissioner of Insurance, shall, on or before the first day of the second month following enactment of this 1990 amendatory and supplementary

act, prepare an estimate of the revenues anticipated to be collected from the surtax imposed pursuant to section 76 of this 1990 amendatory and supplementary act, at the rate established thereby, and credited to the New Jersey Automobile Insurance Guaranty Fund, for each of the three calendar years in which the surtax is imposed. These estimates shall be reviewed and, if appropriate, revised, on or before the first day of the month immediately preceding the due date for the second installment payment for the first calendar year in which the surtax is imposed and each subsequent installment payment and each final payment required to be made pursuant to section 76 of this 1990 amendatory and supplementary act. Such review and revision shall be based upon information available to the director and the commissioner, including actual surtax collections as reflected in final payments.

c. At any time that the estimates prepared and revised pursuant to subsection b. of this section reflect total estimated surtax revenues in excess of, or significantly less than, \$300,000,000 for the three calendar years in which the surtax is imposed, the director shall provide that the surtax be imposed at a different rate, such that the total estimated revenues are as near as possible to, but do not exceed, \$300,000,000, provided, however, that the rate shall not exceed 5%. That different surtax rate shall be imposed on premiums collected in the first calendar year for which final returns and final payments have not yet been made and, subject to the director's determination, may be reflected in installment payments which have not yet been made.

d. On or before April 1, 1993, the director shall make a final determination of the total amount of revenues collected under the surtax imposed pursuant to section 76 of this 1990 amendatory and supplementary act for the three calendar years in which the surtax is imposed. The director shall refund any such revenues collected in excess of \$300,000,000 to taxpayers in proportion to each taxpayer's share of total surtax payments made for the three calendar years.

FAIRA § 78

17:33B-51. Policyholders not to pay surtax

The Commissioner of Insurance shall take such action as is necessary to ensure that private passenger automobile insurance policyholders shall not pay for the surtax imposed pursuant to section 76 of this 1990 amendatory and supplementary act.

FAIRA § 88

17:33B-11. Market Transition Facility; advisory board; membership; plan of operation; apportionment of profits and losses

a. There is created a Market Transition Facility to be operated by the Commissioner of Insurance pursuant to the provisions of this section. Every insurer authorized to transact automobile insurance in this State shall be a

member of the facility and shall share in its profits and losses as provided by the commissioner pursuant to the provisions of subsection d. of this section.

b. The commissioner shall, within 30 days of the effective date of this 1990 amendatory and supplementary act, appoint a Market Transition Facility Advisory Board which shall be comprised of six members, one of whom shall represent member companies organized on a mutual basis, one of whom shall represent member companies organized on a stock basis, one of whom shall represent servicing carriers, one of whom shall represent insurance producers, one of whom shall be a qualified actuary and one of whom shall represent the public. Advisory board members shall serve for the duration of the facility or until such time as their successor is appointed. Advisory board members shall not be compensated for their services but shall be reimbursed by the facility for any necessary and reasonable expenses incurred in performance of their duties as members of the advisory board.

c. The facility shall arrange for the issuance and renewal of automobile insurance policies for the period commencing October 1, 1990 and ending September 30, 1992 pursuant to a plan of operation promulgated by the commissioner in consultation with the advisory board. The facility shall not issue or renew any policies of automobile insurance on or after October 1, 1992. The plan shall provide:

(1) The applicable levels of coverage available through the facility;

(2) That the premiums payable on policies issued by the facility shall be based on rates applicable to persons insured by the New Jersey Automobile Full Insurance Underwriting Association on September 30, 1990 but shall not incorporate the rates applicable under section 25 of P.L.1983, c.65 (C.17:30E-13) and section 22 of P.L.1988, c.119 (C.17:30E-13.1). However, the applicable rates for those insureds who do not qualify as eligible persons as provided in section 25 of this 1990 amendatory and supplementary act shall be those set by the plan for the provision of automobile insurance established pursuant to section 1 of P.L.1970, c.215 (C.17:29D-1);

(3) Procedures for the filing and approval of changes in rates applicable to policies issued or renewed by the facility;

(4) For the insurance and renewal of automobile insurance through servicing carriers under contract with the New Jersey Automobile Full Insurance Underwriting Association pursuant to the provisions of section 24 of P.L.1983, c.65 (C.17:30E-12), utilizing, at the discretion of the commissioner, the staff of the association;

(5) Procedures for the depopulation of the facility which shall provide that: on or after April 1, 1991 no more than 29% of the aggregate number of private passenger non-fleet exposures written in this State shall be written by the facility and the New Jersey Automobile Full Insurance Underwriting Association created by P.L.1983, c.65 (C.17:30E-1 et seq.); on or after October 1, 1991 no more than 20% of the aggregate number of private passenger non-fleet exposures written in this State shall be written by the facility; on or after April 1, 1992 no

more than 10% of the aggregate number of private passenger non-fleet exposures written in this State shall be written by the facility; and on or after October 1, 1992, 0% of the aggregate number of private passenger non-fleet exposures written in this State shall be written by the facility. In establishing the quotas set forth above, the plan shall prescribe the number of voluntary market exposures which shall be written during each six month period set forth in this paragraph in a manner consistent with the apportionment procedure established pursuant to subsection a. of section 26 of P.L.1983, c.65 (C.17:30E-14). In the event that any of the quotas established pursuant to this paragraph have not been met by the end of the applicable period, the commissioner shall direct the facility to assign the balance of the exposures needed to meet the applicable quota to member companies pursuant to the apportionment procedure. A member company which exceeds its apportionment share for any six month period set forth in this paragraph shall receive credit for the excess against the following period's obligation. The commissioner may excuse a member company from meeting its obligations under the depopulation procedures if he determines that the company would be placed in an unsafe or unsound condition;

(6) A schedule for the payment of premiums on an installment basis. Any installment payment schedule for policies issued for one year period shall provide for installment payments during a period of not less than nine months;

(7) That no policy issued by the facility may be cancelled for nonpayment of premium unless written notice is provided at least 15 days prior to the effective

date of cancellation accompanied by the reason for cancellation. Notice shall be provided to the named insured and the producer of record at their last known addresses;

(8) Provided for notification of the named insured and the producer of record at their last known addresses no later than 15 days after the nonrenewal of a facility policy of such nonrenewal; and

(9) Such other provisions as are deemed necessary for the operation of the facility.

d. The commissioner shall apportion any profits or losses of the facility among member companies based on each company's apportionment share as determined for purposes of depopulation pursuant to subsection a. of section 26 of P.L.1983, c.65 (C.17:30E-14).

e. The facility shall be subject to the provisions of P.L.1945, c.132 (C.54:18A-1 et seq.).

New Jersey Statutes Annotated:

N.J.S.A. 17:29A-4. Rates; establishment; considerations

Every rating organization, and every insurer which makes its own rates, shall make rates that are not unreasonably high or inadequate for the safety and soundness of the insurer, and which do not unfairly discriminate between risks in this State involving essentially the same hazards and expense elements, and shall, in rate-making, and in making rating systems:

(a) Adopt basic classifications, which shall be used as the basis of all manual, minimum, class, schedule, experience or merit rates;

(b) Adopt reasonable standards for construction, for protective facilities, and for other conditions that materially affect the hazard or peril, which shall be applied in the determination or fixing of rates;

(c) Give consideration to past and prospective loss experience, including where pertinent, the conflagration and catastrophe hazards, if any, both within and without the State; to all factors reasonably related to the kind of insurance involved; to a reasonable profit for the insurer; and, in the case of participating insurers, to policyholders' dividends. In the case of fire insurance, consideration shall be given to the latest available experience of the fire insurance business during a period of not less than 5 years preceding the year in which rates are made or revised;

(d) Give a rate reduction, to be approved by the commissioner, for fire insurance on structures equipped with operative smoke detection devices of a design approved by the Commissioner of Insurance.

N.J.S.A. 17:29A-14. Alteration of rates: procedure

a. With regard to all property and casualty lines, a filer may, from time to time, alter, supplement, or amend its rates, rating systems, or any part thereof, by filing

with the commissioner copies of such alterations, supplements, or amendments, together with a statement of the reason or reasons for such alteration, supplement, or amendment, in a manner and with such information as may be required by the commissioner. If such alteration, supplement, or amendment shall have the effect of increasing or decreasing rates, the commissioner shall determine whether the rates as altered thereby are reasonable, adequate, and not unfairly discriminatory. If the commissioner shall determine that the rates as so altered are not unreasonably high, or inadequate, or unfairly discriminatory, he shall make an order approving them. If he shall find that the rates as altered are unreasonable, inadequate, or unfairly discriminatory, he shall issue an order disapproving such alteration, supplement or amendment.

b. Deleted by amendment. P.L.1984, c.1

c. If an insurer or rating organization files a proposed alteration, supplement or amendment to its rating system, or any part thereof, which would result in a change in rates, the commissioner may, or upon the request of the filer or the Public Advocate shall, certify the matter for a hearing. The hearing shall, at the commissioner's discretion, be conducted by himself, by a person appointed by the commissioner pursuant to section 26 of P.L.1944, c.27 (C.17:29A-26), or by the Office of Administrative Law, created by P.L.1978, c.67 (C.52:14F-1 et seq.), as a contested case. The following requirements shall apply to the hearing:

(1) The hearing shall commence within 30 days of the date of the request or decision that a hearing is to be

held. The hearing shall be held on consecutive working days, except that the commissioner may, for good cause, waive the consecutive working day requirement. If the hearing is conducted by an administrative law judge, the administrative law judge shall submit his findings and recommendations to the commissioner within 30 days of the close of the hearing. The commissioner may, for good cause, extend the time within which the administrative law judge shall submit his findings and recommendations by not more than 30 days. A decision shall be rendered by the commission not later than 60 days, or, if he has granted a 30 day extension, not later than 90 days, from the close of the hearing. A filing shall be deemed to be approved unless rejected or modified by the commissioner within the time period provided therein.

(2) The commissioner, or the Director of the Office of Administrative Law, as appropriate, shall notify all interested parties, including the Public Advocate on behalf of insurance consumers, if the date set for commencement of the hearing, on the date of the filing of the request for a hearing, or within 10 days of the decision that a hearing is to be held.

(3) The insurer or rating organization making a filing on which a hearing is held shall bear the costs of the hearing.

(4) The commissioner may promulgate rules and regulations (a) to establish standards for the submission of proposed filings, amendments, additions, deletions and alterations to the rating system of filers, which may include forms to be submitted by each filer; and (b)

making such other provisions as he deems necessary for effective implementation of this act.

d. Deleted by amendment. P.L.1984, c.1

e. In order to meet, as closely as possible, the deadlines in section 17 of P.L.1983, c.362 (C.39:6A-23) for provision of notice of available optional automobile insurance coverages pursuant to section 13 of P.L.1983, c.362 (C.39:6A-4.3) and section 8 of P.L.1972, c.70 (C.39:6A-8), and to implement these coverages, the commissioner may require the use of rates, fixed by him in advance of any hearing, for deductible, exclusion, setoff and tort limitation options, on an interim basis, subject to a hearing and to a provision for subsequent adjustment of the rates, by means of a debit, credit or refund retroactive to the effective date of the interim rates. The public hearing on initial rates applicable to the coverages available under section 13 of P.L.1983, c.362 (C.39:6A-4.3) and section 8 of P.L.1972, c.70 (C.39:6A-8) shall not be limited by the provisions of subsection c. of this section governing changes in previously approved rates or rating systems.

N.J.S.A. 17:29A-35. Merit rating accident surcharge for private passenger automobiles; plan; suspension of license; disposition of funds; amount of surcharge; rules and regulations

a. A merit rating accident surcharge system for private passenger automobiles may be used both in the voluntary market and by the New Jersey Automobile Full Insurance Underwriting Association created pursuant to

section 16 of P.L.1983, c.65 (C.17:30E-4). No surcharges shall be imposed on or after the operative date of this act, unless there is an at-fault accident within a three year period immediately preceding the effective date of coverage which results in payment by the insurer of at least a \$300.00 claim. All moneys collected under this subsection shall be retained by the insurer assessing the surcharge. Accident surcharges shall be imposed for a three year period and shall, for each filer, be uniform on a Statewide basis without regard to classification or territory.

b. There is created a New Jersey Merit Rating Plan which shall apply to all drivers and shall include, but not be limited to, the following provisions:

(1)(a) Plan surcharges shall be levied, beginning on or after January 1, 1984, by the Division of Motor Vehicles on any driver who has accumulated, within the immediately preceding three year period, beginning on or after February 10, 1983, six or more motor vehicle points, as provided in Title 39 of the Revised Statutes, exclusive of any points for convictions for which surcharges are levied under paragraph (2) of this subsection; except that the allowance for a reduction of points in title 39 of the Revised Statutes shall not apply for the purpose of determining surcharges under this paragraph. Surcharges shall be levied for each year in which the driver possesses six or more points. Surcharges assessed pursuant to this paragraph shall be not less than \$100.00 for six points, and not less than \$25.00 for each additional point. The commissioner may increase the amount of surcharges as he deems necessary to effectuate the purposes of subsection d. of this section and P.L.1983, c.65 (C.17:29A-33 et al.), and may, pursuant to regulation, permit the deferral

of all or part of any surcharges authorized by this subsection until the end of the policy term of an automobile insurance policy with an effective date prior to January 1, 1984, upon presentation of appropriate evidence that an insured has already paid an equivalent surcharge arising from the same motor vehicle violation or conviction.

(b) (Deleted by amendment, P.L.1984, c.1.)

(2) Plan surcharges shall be levied for convictions (a) under R.S. 39:4-50 for violations occurring on or after February 10, 1983, and (b) under section 2 of P.L.1981, c.512 (C.39:4-50.4a), or for offenses committed in other jurisdictions of a substantially similar nature to those under R.S. 39:4-50 or section 2 of P.L.1981, c.512 (C.39:4-50.4a), for violations occurring on or after January 26, 1984. Surcharges under this paragraph shall be levied annually for a three year period, and shall be not less than \$1,000.00 per year for each of the first two convictions, and not less than \$1,500.00 per year for the third conviction occurring within a three year period. If a driver is convicted under both R.S.39:4-50 and section 2 of P.L.1981, c.512 (C.39:4-50.4a) for offenses arising out of the same incident, the driver shall be assessed only one surcharge for the two offenses. The commissioner may increase the amount of surcharges as he deems necessary to effectuate the purposes of subsection d. of this section and P.L.1983, c.65 (C.17:29A-33 et al.), and may, pursuant to regulation, permit the deferral of all or any part of these surcharges as provided in paragraph (1)(a) of this subsection.

If, upon written notification from the Division of Motor Vehicles, mailed to the last address of record with the division, a driver fails to pay a surcharge levied

under this subsection, the license of the driver shall be suspended forthwith until the surcharge is paid to the Division of Motor Vehicles; except that upon satisfactory showing of indigency, the Division of Motor Vehicles may authorize payment of the surcharge on an installment basis over a period not to exceed 10 months.

For the purposes of this subparagraph, "indigency" shall be defined in rules and regulations promulgated by the Director of the Division of Motor Vehicles.

All moneys collectible under this subsection shall be billed and collected by the Division of Motor Vehicles. Of the moneys collected, 10%, or the actual cost of administering the collection of the surcharge, whichever is less, shall be retained by the Division of Motor Vehicles and turned over to the State Treasury for deposit in a special account to be used by the Division of Motor Vehicles, as may be necessary, to modernize its operations and improve its effectiveness and efficiency in order to discharge its statutory obligations and the remainder shall be remitted to the New Jersey Automobile Full Insurance Underwriting Association. Any moneys in the special account at the end of a fiscal year shall be transferred to the General Fund for use for general State purposes. Moneys shall be appropriated annually to the special account.

(3) In addition to any other authority provided in P.L.1983, c.65 (C.17:29A-33 et al.), the commissioner, after consultation with the Director of the Division of Motor Vehicles, is specifically authorized (a) to increase the dollar amount of the surcharges for motor vehicle violations or convictions, (b) to impose, in accordance with paragraph (1)(a) of this subsection, surcharges for motor

vehicle violations or convictions for which motor vehicle points are not assessed under Title 39 of the Revised Statutes, or (c) to reduce the number of points for which surcharges may be assessed below the level provided in paragraph (1)(a) of this subsection, except that the dollar amount of all surcharges levied under the New Jersey Merit Rating Plan shall be uniform on a Statewide basis for each filer, without regard to classification or territory. Surcharges adopted by the commissioner on or after January 1, 1984 for motor vehicle violations or convictions for which motor vehicle points are not assessable under Title 39 of the Revised Statutes shall not be retroactively applied but shall take effect on the date of the New Jersey Register in which notice of adoption appears or the effective date set forth in that notice, whichever is later.

c. No motor vehicle violation surcharges shall be levied on an automobile insurance policy issued or renewed on or after January 1, 1984, except in accordance with the New Jersey Merit Rating Plan, and all surcharges levied thereunder shall be assessed, collected and distributed in accordance with subsection b. of this section.

d. The dollar amount of all motor vehicle conviction surcharges shall be at least equivalent to the differential between the rates charged to insureds as promulgated by the rating bureau which files rates for the greatest number of insurers in the voluntary private passenger automobile insurance market in this State and the Supplement I rates in use as of December 31, 1982 by the automobile insurance plan established pursuant to P.L.1970, c.215 (C.17:29D-1), and the amount collectible under the motor vehicle conviction surcharge system in use by the automobile insurance plan established pursuant to P.L.1970, c.215 (C.17:29D-1 et seq.) prior to the

implementation of this act; except that in the first year of operation of the New Jersey Automobile Full Insurance Underwriting Association, the dollar amount of all motor vehicle surcharges shall be sufficient to eliminate the need for imposition of a residual market equalization charge authorized under section 20 of P.L.1983, c.65 (C.17:30E-8).

e. The Commissioner of Insurance and the Director of the Division of Motor Vehicles as may be appropriate, shall adopt any rules and regulations necessary or appropriate to effectuate the purposes of this section.

N.J.S.A. 17:29A-36. Filing for automobile insurance rate making

Any filing made for the purpose of automobile insurance rate making shall indicate the actual rate needs of the filer, provided, however, that (a) each filer's rate classification definitions, as used by that filer, shall be uniform Statewide; (b) the automobile insurance rate charged an insured shall not exceed two and one-half times the filer's territorial base rate for each coverage, exclusive of driving record surcharges and discounts; and (c) the automobile insurance rate for the base class in any territory for any filer shall not exceed 1.35 times the filer's Statewide average base rate for each coverage, exclusive of driving record surcharge and discounts. The automobile insurance rate of an automobile whose principal operator is 65 years of age or older shall not exceed one and one-quarter times the Statewide average rate for principal operators 65 years of age or older for each

coverage, exclusive of driving record surcharges and discounts; provided, however, that no filer shall increase rates for principal operators 65 years of age or older as a result of the implementation of this section unless more than 50% of its insureds are principal operators 65 years of age or older.

As used in this section, base rate means the automobile insurance rate charged for an automobile that is not used in business and not used in going to and from work except for the going to and from work distance included in the pleasure use classification of the filer, and where there is no youthful operator, as defined in the filer's classification system. The base rate class shall not include automobiles to which discounts apply under the filer's classification system, including, but not limited to, farmer's and senior citizen's automobiles.

The provisions of this section shall be implemented after the implementation of the provisions of subsection a. of section 8 of this act.

N.J.S.A. 17:29A-44. Maximum rates

a. Beginning July 1, 1989, a filer may charge rates for private passenger automobile insurance in the voluntary market which are not in excess of the following:

(1) For private passenger automobile personal injury protection coverage, residual bodily injury and property damage insurance, the maximum permissible annual rate increase applicable to each rate level utilized

by an insurer in the voluntary market pursuant to section 6 of P.L.1988, c.156 (C.17:29A-45) shall be a Statewide average rate change of not more than the last published increase in the medical care services components of the national Consumer Price Index, all urban consumers, U.S. city average, plus three percentage points.

(2) For private passenger automobile physical damage coverage, the maximum permissible annual rate increase applicable to each rate level utilized by an insurer in the voluntary market pursuant to section 6 of P.L.1988, c.156 (C.17:29A-45) shall be a Statewide average rate change of not more than the last published increase in the automobile maintenance and repair components of the national Consumer Price Index, U.S. city average, plus three percentage points.

b. For the purposes of this section, "Statewide average rate change" means the total Statewide premium for all coverages at the rates in effect at the time of the filing for each rate level.

c. Any change-in excess of the rate changes permitted by paragraphs (1) and (2) of subsection a. shall be subject to the provisions of P.L.1944, c.27 (C.17:29A-1 et seq.).

d. If, at any time, the commissioner believes that an increase in either or both of the published indices will produce rate levels which are excessive, he may modify the Statewide average rate change which may be used pursuant to this section.

e. A filer may implement a change in rate level, pursuant to subsection a. of this section, in whole or in part, in a single or in multiple filings by making an informational filing with the commissioner in a manner and form approved by the commissioner. The filing shall include a statement of the reason or reasons for the change in rate level, including, but not limited to, the claim and expense experience of the individual filer.

f. Other than filings made pursuant to subsection c. of this section, neither the provisions of subsection c. of section 14 of P.L.1944, c.27 (C.17:29A-14), nor the provisions of section 19 of P.L.1974, c.27 (C.52:27E-18), shall apply to any filing made pursuant to this section. However, the commissioner shall provide a copy of any filing made or other information provided by a filer pursuant to the provisions of this section to the Department of the Public Advocate, Division of Rate Counsel. The Public Advocate may challenge a rate change implemented pursuant to subsection a. of this section after the effective date of the rate change by filing such challenge in writing with the commissioner within 30 days of the effective date of the rate change. The commissioner shall hear the matter on an expedited basis and shall render a final determination within six months of the date of filing. The commissioner may, for good cause, extend this six-month period up to an additional three months. If the Public Advocate prevails, the commissioner shall reduce or rescind the rate change as appropriate. If the commissioner reduces or rescinds a rate change as a result of a challenge by the Public Advocate filed pursuant to the provisions of this subsection, the filer shall bear the cost

of the reasonable expenses incurred by the Public Advocate in maintaining the challenge.

g. The Commissioner shall monitor the implementation and use of flex rating pursuant to this section and shall report his findings to the Senate Labor, Industry and Professions Committee and the Assembly Insurance Committee, or their successors, including any legislative proposals, no later than July 1, 1992. This report shall provide an evaluation of the use of this rating mechanism and its impact on the availability and affordability of private passenger automobile insurance in this State and the depopulation of the New Jersey Automobile Full Insurance Underwriting Association and shall include any legislative proposals or other recommendations of the commissioner.

N.J.S.A. 17:29C-7.1. Refusal to renew policy with coverage under provisions of Automobile Reparation Reform Act; conditions

a. Notwithstanding the provisions of section 3 of P.L.1972, c.70 (C.39:6A-3), a licensed insurer may, in accordance with subsections b. and c. of this section, refuse to renew a policy of private passenger automobile insurance that provides coverage required to be maintained pursuant to P.L.1972, c.70 (C.39:6A-1 et seq.).

b. For each calendar year period, an insurer may issue notices of intention not to renew an automobile insurance policy in the voluntary market in an amount not to exceed 2% of the total number of voluntary market automobile insurance policies of the insurer, rounded to the nearest whole number, which are in force at the end

of the previous calendar year in each of the insurer's rating territories in use in this State.

c. For every two newly insured automobiles which an insurer voluntarily writes in each territory during each calendar year period, the insurer shall be permitted to refuse to renew one additional policy of automobile insurance in that territory in excess of the 2% limitation established by subsection b. of this section, subject to a fair and nondiscriminatory formula developed by rule or regulation of the commissioner. For the purposes of this section, "voluntarily writes" shall not include any exposure voluntarily written by or assigned to an insurer to meet any quota established pursuant to section 26 of P.L.1983, c.65 (C.17:30E-14).

d. The provisions of this section shall not apply to any cancellation made pursuant to subsection (A) of section 2 of P.L.1968, c.158 (C.17:29C-7).

e. The commissioner shall monitor the implementation and operation of this section and shall report his findings, including any legislative proposals, to the Senate Labor, Industry and Professions Committee and the Assembly Insurance Committee, or their successors, within three years of the effective date of this act.

N.J.S.A. 17:29D-1. Rules and regulations

The Commissioner of Insurance may adopt, issue and promulgate rules and regulations establishing a plan for

the providing and apportionment of insurance coverage for applicants therefor who are in good faith entitled to, but are unable to procure the same, through ordinary methods. Every insurer admitted to transact and transacting any line, or lines, of insurance in the State of New Jersey shall participate in such plan and provide insurance coverage to the extent required in such rules and regulations.

Any plan established pursuant to this section to provide insurance for automobiles, as defined in section 2 of P.L.1972, c.70 (C.39:6A-2), shall provide:

a. That any automobile liability insurance coverage with limits in excess of \$50,000 per person and \$100,000 per accident for bodily injury or death and \$25,000 for property damage, or in lieu thereof, \$100,000 for a single limit of liability against claims for bodily injury or death and property damage, shall be experience rated with respect to the rate applicable to coverage in excess of those limits;

b. That collision and comprehensive automobile insurance coverages on automobiles with a value of \$25,000 or more at the time those coverages are issued or renewed shall be experience rated and for automobiles with a value of more than \$15,000 but less than \$25,000 at the time those coverages are issued or renewed that part of the rate applicable to the value between \$15,000 and \$25,000 shall be experience rated;

c. For a limited assignment distribution system permitting insurers to enter into agreements with other mutually agreeable insurers or other qualified entities to

transfer their applicants and insureds under such plan to such insurers or other entities;

d. That it shall not provide insurance coverage for more than 10 percent of the aggregate number of private passenger automobile non-fleet exposures being written in the total private passenger automobile insurance market in this State. The plan shall provide for the cessation of the acceptance of applications or the issuance of new policies at any time it reaches 10 percent of marketshare, as certified by the commissioner, until such time that the commissioner certifies that the plan is insuring less than 10 percent of the aggregate number of private passenger automobile non-fleet exposures being written in the total private passenger automobile insurance market in this State;

e. That it shall not provide coverage to an eligible person as defined pursuant to section 25 of P.L.1990, c.8 (C.17:33B-13); and

f. That insurers who write automobile risks in those urban territories designated by the commissioner shall receive one assigned risk credit for every two voluntary risks written in those designated territories.

Prior to the adoption or amendment of such rules and regulations, the commissioner shall consult with such members of the insurance industry as he deems appropriate. Such consultation shall be in addition to any otherwise required public hearing or notice with regard to the adoption or amendment of rules and regulations.

N.J.S.A. 17:30E-2. Purpose of act

The purpose of this act is to assure to the New Jersey insurance consumer full access to automobile insurance through normal market outlets, to encourage the use of available market facilities, to provide automobile insurance for qualified applicants who cannot otherwise obtain such insurance, through a full automobile insurance underwriting association, and to require that companies be made whole for losses in excess of regulated rates on all risks not voluntarily written by providing procedures for the spreading and recoupment of losses based on actual experience.

N.J.S.A. 17:30E-3(o). Definitions

As used in sections 13 to 34 of this act:

* * *

o. "Residual market equalization charge" means the amount imposed pursuant to section 20 of P.L. 1983, c.65 (C.17:30E-8) which, when added to other sources of association income, will cause the association to operate on a no profit, no loss basis.

N.J.S.A. 17:30E-6. Plan of operation

a. Within 90 days after the organizational meeting, unless after the sixtieth day, but not later than the

seventieth day, following the organizational meeting, the commissioner for good cause grants an additional period not to exceed 30 days, the board shall file with the commissioner for his approval a proposed plan of operation, consistent with the provisions of this act, which shall provide for the prompt and efficient provision of automobile insurance to qualified applicants. The plan of operation shall provide for, among other matters, methods and means for the collection, investment and disbursement of funds; methods and standards for the establishment of adequate, actuarially sound reserves for unpaid losses, including provision for incurred but not reported losses; reasonable and adequate commissions to producers; protection of the interests of producers of record without a contractual relationship with a voluntary market member company; procedures and methods for issuing policies on behalf of the association; the method for determining and means of assessing the liability of an insurer which ceases to transact automobile insurance in this State with respect to business transacted prior to the effective date of its termination of membership; minimum requirements for the selection and performance of servicing carriers; minimum requirements for the performance of producers; reasonable and adequate compensation of such servicing carriers; procedures for matching producers with servicing carriers; the methods and procedures for notifying directors of the time and place of board meetings; and the phasing out of the plan for the providing and apportionment of automobile insurance pursuant to section 1 of P.L.1970, c.215 (C.17:29D-1), in a manner which will minimize the shifting of insureds among carriers, except that nothing

herein shall be interpreted to affect the provisions of P.L.1968, c.158 (C.17:29C-6 et seq.).

b. The plan of operation adopted by the board shall be submitted to the commissioner for his review and approval. If the commissioner approves the proposed plan, he shall certify such approval to the directors and said plan shall take effect on the date certified by the commissioner. If the commissioner disapproves all or any part of the proposed plan of operation, he shall return same to the directors with a statement, in writing, of the reasons for his disapproval and any recommendations he may wish to make. The directors may accept the commissioner's recommendations or may propose a new plan, which recommendations or plan shall be submitted to the commissioner within 30 days after the return of a disapproved plan to the directors. If the directors do not submit a proposed plan of operation or if the directors do not submit a new plan which is acceptable to the commissioner, or accept the recommendations of the commissioner within 30 days after the disapproval of a proposed plan, the commissioner shall promulgate a plan of operation and certify same to the directors. Any such plan promulgated by the commissioner shall take effect on the date certified by the commissioner.

c. The directors of the association may amend the plan of operation at any time, subject to approval by the commissioner.

d. The commissioner shall annually review the plan of operation and, not later than April 1, 1985 and not later than April 1 of each year thereafter, shall approve or amend the plan of operation; and any amendments to the

plan adopted by the commissioner pursuant to the annual review shall be binding on the board as of the effective date of the amendments. The commissioner may review the plan of operation at any other time, and may propose amendments to the board. If the board does not adopt amendments acceptable to the commissioner within 30 days, the commissioner may certify amendments and their effective date to the board.

e. Any order of the commissioner with respect to the plan of operation, or any amendment thereto, shall be subject to review by the Appellate Division of the Superior Court.

N.J.S.A. 17:30E-8. Sources of income; claims; filing of experiences; residual market equalization charge; membership in association

a. — The association shall derive income from the following sources for the payment of expenses, losses, and the provision of adequate, actuarially sound reserves for unpaid losses and loss adjustment expenses, including incurred but not reported losses, in connection with association business: (1) net premiums earned; (2) income generated from any association accident surcharge system permitted or required by law; (3) that percentage of surcharges collected by the Division of Motor Vehicles prior to October 1, 1991 and deposited with the association pursuant to subsection b. of section 6 of the "New Jersey Automobile Insurance Reform Act of 1982," (~~P.L.1983, c.65; C.17:29A-35~~) P.L.1983, c.65 (C.17:29A-35);

(4) income collected by members of the association and by the association from the residual market equalization charge imposed prior to April 1, 1991, or flat charges (also referred to as capitation fees or policy constants, but not including premiums for uninsured motorist or towing coverage, or flattened tax and expense fees implemented pursuant to section 8 of P.L.1983, c.65 (C.17:29A-37)) imposed prior to April 1, 1991, levied on a per car and per coverage basis; ~~and~~ (5) income from investment of moneys collected pursuant to paragraphs (1), (2), (3), ~~and~~ (4) and (6) of this subsection; and (6) income collected by the Director of the Division of Motor Vehicles prior to October 1, 1991, pursuant to section 68 of P.L.1991, c.8 (C.17:33B-63). Residual market equalization charges collected on behalf of the association shall on a monthly basis be certified to by the carrier and shall be transferred to the association in accordance with the plan of operation. No producer commissions or premium taxes shall be paid on, or company expenses or servicing carrier compensation deducted from the residual market equalization charge. No servicing carrier compensation or commissions shall be paid by the association on violation surcharges deposited by the Division of Motor Vehicles with the association. All premiums received by servicing carriers on behalf of the association shall on a monthly basis be certified to by the carrier and shall be transferred to the association in accordance with the plan of operation. Premiums shall be transferred to the association net of commissions paid, all premium taxes, and servicing carrier compensation, except as otherwise required by law.

All claims and claim expense payments paid on association business shall be disbursed by the servicing carriers or the association through drafts drawn on association funds in accordance with the plan of operation. Servicing carriers, as agents of the association, shall have no individual liability on claims or policies written by the association.

b. At least annually, the board shall file its experience with the commissioner, which experience shall include the projected income, expenses, losses and reserve requirements of the association for the ensuing year, any adjustment in previously established reserves for unpaid losses and loss adjustment expenses necessary to make such reserves adequate and actuarially sound, and the initial filing shall include the experience of the automobile insurance plan established pursuant to P.L.1970, c.215 (C.17:29D-1). Except in the case of the initial or other filing applicable to the first year of operation of the association, the board shall include in its filing with the commissioner, for his approval, a computation of the residual market equalization charge per insured vehicle to be collected by each member from its voluntary insureds, exclusive of principal operators 65 years of age or older, and by each servicing carrier from association insureds or insureds covered by the Market Transition Facility created pursuant to section 88 of P.L.1990, c.8 (C.17:33B-11), exclusive of principal operators 65 years of age or older, to offset the anticipated losses of the association.

At the end of the first 12 months of the operation of the association and at least annually thereafter, the board shall also include in its filing with the commissioner a

review of the previous year's experience, setting forth the income, losses, and reserve requirements, including any adjustment in previously established reserves for unpaid losses and loss adjustment expenses necessary to make such reserves adequate and actuarially sound, and expenses of the association during the previous year. ~~If a profit is found by the commissioner to have been realized, such amount shall reduce the residual market equalization charge levied on policyholders pursuant to subsection d, of this section. If a loss is found by the commissioner to have occurred, such amount shall increase the charge levied on policyholders pursuant to subsection d, of this section.~~ The filing shall be accompanied by such statistics and other information as the commissioner may deem necessary. The commissioner shall, within 60 days of such filing, approve or disapprove the filing, except that the commissioner may, for good cause, extend by not more than 60 days the period for approving or disapproving the filing. Failure to act within the period allowed for the commissioner's review of the filing shall be deemed approval of the filing, except that the running of the period shall be tolled by a request for additional information by the commissioner or until the association notifies the commissioner that it will not provide such additional information, together with the reason for not supplying the information. Failure to comply with a reasonable request for information may be a ground for disapproving all or part of the filing. If the commissioner disapproves all or part of the filing, he shall state the reasons for such disapproval, and indicate such portion of the filing he approves. Such disapproval

shall be subject to review by the Appellate Division of the Superior Court.

* * *

N.J.S.A. 17:30E-8.1. Plan for payment of obligations if resources insufficient; approval; plan for deferral of payments of property damage claims subject to subrogation

a. Beginning January 1, 1989 and annually thereafter, the commissioner shall determine whether the income of the association as provided for in paragraphs (1), (2), (3), and (5) of section 20 of P.L.1983, c.65 (C.17:30E-8), and the residual market equalization charge levied pursuant to paragraph (4) of that section prior to the effective date of this 1988 amendatory and supplementary act is or will be sufficient to meet its obligations in the ensuing year. If the commissioner determines that the association has insufficient resources to meet its obligations, he shall request the board of the association to formulate a plan for the payment of no less than 50% of the aggregate residual bodily injury losses for which the association is to make payment during the ensuing 12 month period, which plan shall provide for the payment of these losses in no more than four annual installments. The board shall submit the plan to the commissioner for his approval. Interest on the balance of the unpaid claim shall be paid at the rate established by subsection (a) of R.S.31:1-1 for loans in which there is no written contract.

b. In addition to the plan provided for in subsection a. of this section, the commissioner may also request the submission of a plan by the board for the deferral, for a period not to exceed twelve months, of payments by the association of property damage claims which are subject to subrogation.

c. No residual market equalization charge in excess of the charge levied prior to the effective date of this 1988 amendatory and supplementary act shall be approved by the commissioner unless the procedures established pursuant to subsection a. or b. of this section do not provide sufficient revenue for the association to pay its obligations.

N.J.S.A. 17:30E-13. Rates

Notwithstanding the provisions of section 7 of P.L.1983, c.65 (C.17:29A-36), the rates used by the association shall be as follows:

a. On January 1, 1989, the territorial base rates used by the association for policies issued or renewed following that date for qualified applicants or association insureds who, for the three years preceding the date of issuance or renewal, (1) have been convicted of two or more moving violations, or have received four or more motor vehicle points, whichever is less; or (2) have had one or more at-fault accidents shall be adjusted by the commissioner so that they exceed the territorial base rates under the rating plan for standard insureds which is

used by the rating bureau which files rates for the greatest number of insurers transacting private passenger automobile insurance in the voluntary market in this State by 10%. Qualified applicants or association insureds who have not had such accidents or moving violations or motor vehicle points in the three years preceding the issuance or renewal shall be rated under the rating plan for standard insureds which is used by the rating bureau which files rates for the greatest number of insurers transacting private passenger automobile insurance in the voluntary market in this State.

b. On January 1, 1990, the territorial base rates used by the association for policies issued or renewed following that date for qualified applicants or association insureds who, for the three years preceding the date of issuance or renewal, (1) have been convicted of two or more moving violations, or have received four or more motor vehicle points, whichever is less; or (2) have had one or more at-fault accidents shall be adjusted by the commissioner based on the needs of the association pursuant to a filing made with the commissioner by the association no later than October 1, 1989. The commissioner may adjust the association rates so that they exceed the territorial base rates under the rating plan for standard insureds which is used by the rating bureau which files rates for the greatest number of insurers transacting private passenger automobile insurance in the voluntary market in this State by no more than 20%, unless the commissioner reduces the amount of the rate increase based on his certification as to the needs of the association on that date. Qualified applicants or association insureds who have not had such accidents or moving

violations or motor vehicle points in the three years preceding the issuance or renewal shall be rated under the rating plan for standard insureds which is used by the rating bureau which files rates for the greatest number of insurers transacting private passenger automobile insurance in the voluntary market in this State.

c. On January 1, 1991, the territorial base rates used by the association for policies issued or renewed following that date for qualified applicants or association insureds who, for the three years preceding the date of issuance or renewal, (1) have been convicted of two or more moving violations, or have received four or more motor vehicle points, whichever is less; or (2) have had one or more at-fault accidents shall be adjusted by the commissioner ~~based on the needs of the association pursuant to a filing made with the commissioner by the association no later than October 1, 1990. The commissioner may adjust the association rates~~ so that they exceed the territorial base rates under the rating plan for standard insureds which is used by the rating bureau which files rates for the greatest number of insurers transacting private passenger automobile insurance in the voluntary market in this State by no more than 30%, unless the commissioner reduces the amount of the rate increase based on his certification as to the needs of the association on that date. Qualified applicants or association insureds who have not had such accidents or moving violations or motor vehicle points in the three years preceding the issuance or renewal shall be rated under the rating plan for standard insureds which is used by the rating bureau which files rates for the greatest number of

insurers transacting private passenger automobile insurance in the voluntary market in this State.

d. On January 1, 1992, the territorial base rates used by the association for policies issued or renewed following that date for qualified applicants or association insureds who, for the three years preceding the date of issuance or renewal, (1) have been convicted of two or more moving violations, or have received four or more motor vehicle points, whichever is less; or (2) have had one or more at-fault accidents shall be adjusted by the commissioner ~~based on the needs of the association pursuant to a filing made with the commissioner by the association no later than October 1, 1991. The commissioner may adjust the association rates~~ so that they exceed the territorial base rates under the rating plan for standard insureds which is used by the rating bureau which files rates for the greatest number of insurers transacting private passenger automobile insurance in the voluntary market in this State by no more than 40%, unless the commissioner reduces the amount of the rate increase based on his certification as to the needs of the association on that date. Qualified applicants or association insureds who have not had such accidents or moving violations or motor vehicle points in the three years preceding the issuance or renewal shall be rated under the rating plan for standard insureds which is used by the rating bureau which files rates for the greatest number of insurers transacting private passenger automobile insurance in the voluntary market in this State.

e. On January 1, 1993, the commissioner shall direct the board to prepare, adopt and file with the commissioner rates which are based upon past and prospective

loss experience of the risks underwritten by the association and the expenses attendant thereto, and which maintain the association on a self-sustaining basis. The commissioner shall approve or disapprove the rates filed by the board pursuant to the provisions of P.L.1944, c.27 (C.17:29A-1 et seq.).

Nothing contained in this subsection shall be deemed to affect the commissioner's ability to continue to maintain any flat charges (also known as flat capitation fees or policy constants) pursuant to section 1 of P.L.1984, c.1 (C.17:29A-37.1) or any residual market equalization charge pursuant to section 20 of P.L.1983, c.65 (C.17:30E-8) approved on or before 48 months following the effective date of this 1988 amendatory and supplementary act.

f. Nothing contained in subsections a. through e. of this section shall operate to cause the rates charged by the association to result in revenues to the association which exceed the needs of the association in meeting its obligations and expenses.

g. The commissioner may order the adjustment of association rates in any territory in which the relationship between the rates used by the association and the rates used by insurers in the standard voluntary market is such that the voluntary market is adversely affected.

h. The commissioner may order the establishment of association rates which are higher than the rates which are otherwise provided for by this section, which rates would be applicable to certain drivers, based on their accident or violation records. The rates applicable to these drivers shall be established additively to the rates

otherwise authorized for the use of the association, shall be spread equably across all classes and territories and may, at the discretion of the commissioner, vary as to the extent of the at-fault accident or violation records of the drivers.

N.J.S.A. 39:6A-2. Definitions

As used in this act:

a. "Automobile" means a private passenger automobile of a private passenger or station wagon type that is owned or hired and is neither used as a public or livery conveyance for passengers nor rented to others with a driver; and a motor vehicle with a pickup body, a delivery sedan, a van, or a panel truck or a camper type vehicle used for recreational purposes owned by an individual or by husband and wife who are residents of the same household, not customarily used in the occupation, profession or business of the insured other than farming or ranching. An automobile owned by a farm family copartnership or corporation, which is principally garaged on a farm or ranch and otherwise meets the definitions contained in this section, shall be considered a private passenger automobile owned by two or more relatives resident in the same household.

b. "Essential services" means those services performed not for income which are ordinarily performed by an individual for the care and maintenance of such individual's family or family household.

c. "Income" means salary, wages, tips, commissions, fees and other earnings derived from work or employment.

d. "Income producer" means a person who, at the time of the accident causing personal injury or death, was in an occupational status, earning or producing income.

e. "Medical expenses" means expenses for medical treatment, surgical treatment, dental treatment, professional nursing services, hospital expenses, rehabilitation services, X-ray and other diagnostic services, prosthetic devices, ambulance services, medication and other reasonable and necessary expenses resulting from the treatment prescribed by persons licensed to practice medicine and surgery pursuant to R.S.45:9-1 et seq., dentistry pursuant to R.S.45:6-1 et seq., psychology pursuant to P.L.1966, c.282 (C.45:14B-1 et seq.) or chiropractic pursuant to P.L.1953, c.233 (C.45:9-41.1 et seq.) or by persons similarly licensed in other states and nations or any non-medical remedial treatment rendered in accordance with a recognized religious method of healing.

f. "Hospital expenses" means:

- (1) The cost of a semiprivate room, based on rates customarily charged by the institution in which the recipient of benefits is confined;
- (2) The cost of board, meals and dietary services;
- (3) The cost of other hospital services, such as operating room; medicines, drugs, anesthetics; treatments with X-ray, radium and other radioactive substances; laboratory tests, surgical

dressings and supplies; and other medical care and treatment rendered by the hospital;

(4) The cost of treatment by a physiotherapist;

(5) The cost of medical supplies, such as prescribed drugs and medicines; blood and blood plasma; artificial limbs and eyes; surgical dressings, casts, splints, trusses, braces, crutches; rental of wheelchair, hospital bed or iron lung; oxygen and rental of equipment for its administration.

g. "Named insured" means the person or persons identified as the insured in the policy and, if an individual, his or her spouse, if the spouse is named as a resident of the same household, except that if the spouse ceases to be a resident of the household of the named insured, coverage shall be extended to the spouse for the full term of any policy period in effect at the time of the cessation of residency.

h. "Pedestrian" means any person who is not occupying, entering into, or alighting from a vehicle propelled by other than muscular power and designed primarily for use on highways, rails and tracks.

i. "Noneconomic loss" means pain, suffering and inconvenience.

j. "Motor vehicle" means a motor vehicle as defined in R.S.39:1-1, exclusive of an automobile as defined in subsection a. of this section.

N.J.S.A. 39:6A-3. Compulsory automobile insurance coverage; limits

Every owner or registered owner of an automobile registered or principally garaged in this State shall maintain automobile liability insurance coverage, under provisions approved by the Commissioner of Insurance, insuring against loss resulting from liability imposed by law for bodily injury, death and property damage sustained by any person arising out of the ownership, maintenance, operation or use of an automobile wherein such coverage shall be at least in:

a. an amount or limit of \$15,000.00, exclusive of interest and costs, on account of injury to, or death of, one person, in any one accident; and

b. an amount or limit, subject to such limit for any one person so injured or killed, of \$30,000, exclusive of interest and costs, on account of injury to or death of, more than one person, in any one accident; and

c. an amount of limit of \$5,000.00, exclusive of interest and costs, for damage to property in any one accident.

No licensed insurance carrier shall refuse to renew the required coverage stipulated by this act of an eligible person as defined in section 25 of P.L.1990, c.8 (C.17:33B-13) except in accordance with the provisions of section 26 of P.L.1988, c.119 (C.17:29C-7.1) or with the consent of the Commissioner of Insurance.

N.J.S.A. 39:6A-18. Mandatory reduction of bodily injury insurance rates

Bodily injury insurance rates in effect on July 1, 1972 shall be reduced by a least 15% and shall become effective upon the effective date of this act.

New Jersey Administrative Code:

N.J.A.C. 11:3-8.3 Standards of nonrenewal applicable to all automobile policies

(a) An insurer may issue notice of nonrenewal based upon one or more of the following reasons:

1. Accident involvement: The named insured or any operator who customarily operates the automobile has been involved during the 36 months period ended 90 days prior to the expiration of the current policy in:

i. Two or more bodily injury accidents if there is one car in the household or three or more accidents if there are at least two cars in the household, provided a loss payment has been made or a loss reserve has been established for such accidents other than a payment for the personal injury protection benefits; or

ii. Two or more accidents involving damage to any property including his own of \$300.00 or more for which accidents a payment was made if there is one car in the household, or three or more such accidents if there are at least two cars in the household, provided that loss payments under the comprehensive physical damage coverage shall not be counted; or

iii. A bodily injury and a physical damage accident as described in i. and ii. above if there is one car in the household. Two bodily injury and one physical damage accident or two physical damage and one bodily injury accident if there are at least two cars in the household.

2. Exceptions: Accidents under i. to iii. above shall not be counted if the accident occurred under the following circumstances:

i. The accident resulted in a claim or payment only under the Personal Injury Protection Coverage;

ii. The automobile was lawfully parked at the time of the accident (an automobile rolling from a parked position shall not be considered as lawfully parked, but shall be considered as in the operation of the last operator);

iii. The named insured or anyone customarily operating the automobile, has been reimbursed by, or on behalf of, a person responsible for the accident or has a judgment against such persons;

iv. The automobile of the named insured or other customary operator was struck in the rear by another vehicle, and the operator has not been convicted of a moving traffic violation in connection with the accident.

v. The operator of another automobile involved in such accident was convicted for a moving traffic violation and the named insured or other customary operator was not convicted of a moving traffic violation in connection therewith;

vi. The automobile operated by the named insured or anyone who customarily operates the automobile is damaged as a result of contact with a "hit and run"

driver, provided that the accident has been reported to legal authorities within a reasonable time thereafter;

vii. The accident resulted from contact with animals or fowl.

3. Convictions concerning motor vehicle law: The named insured or any operator who customarily operates the automobile:

i. Has been convicted, entered a plea of guilty or nolo contendere, forfeited bail bond or other security for any one of the following motor vehicle law violations during the 36 months ended 90 days prior to the expiration date of the current policy:

(1) Driving while intoxicated or under the influence of drugs;

(2) Leaving the scene of an accident;

(3) Criminal negligence or assault arising out of the operation of a motor vehicle;

(4) Driving while license is suspended or revoked.

ii. Has been convicted, entered a plea of guilty or nolo contendere, or forfeited bail bond or other security for other moving traffic violations during the 36 months period ended 90 days prior to the expiration of the current policy which result in the accumulation of an average of nine points or more, as defined in the New Jersey Motor Vehicle Law, per car in the household or which result in an accumulation of nine or more points for any one such operator, provided that any operator who has

been involved in such motor vehicle law violations continues to be an operator or the automobile at the time of renewal.

4. Convictions other than motor vehicle laws: The named insured or anyone customarily operating the automobile is convicted, entered a plea of guilty or nolo contendere, forfeited bail bond or other security for obtaining or attempting to obtain from any other person, insurance company of the Unsatisfied Claim and Judgment Fund any money or any other thing of value by falsely or fraudulently representing that such person is entitled to such consideration under the automobile insurance policy, or falsely or fraudulently making statement or presenting documentation in order to obtain such consideration, or by cooperating, conspiring or otherwise acting in concert with any person seeking to obtain or attempting to obtain falsely or fraudulently such consideration.

5. Use of the automobile in professional racing.

6. Physical or mental impairment of the named insured or anyone customarily operating the automobile which adversely affects the ability to operate the automobile safely, unless a physical disability is compensated for by corrective measures.

i. A nonrenewal premised upon physical or mental impairment must be supported by a current medical examination. The medical examination report must clearly state the nature of the impairment and, in the case of a physical disability, the extent to which such disability adversely affects the ability to safely operate the automobile. In the event such a current medical examination

report is not otherwise available, it must be secured by the insurer at its own expense.

7. Refusal to submit to a medical examination at company expense where there is reason for the company to doubt an operator's ability to operate the automobile safely.

8. Addition of an operator of the automobile during the policy term or for the new policy term with respect to whom any of the above causes for nonrenewal would apply.

9. In the case of companies which limit their writing to members of a church, profession or occupation or similar group, loss of the qualification for such group by the owner of the automobile. In such case an additional 12 months of nonrenewal notice shall be given. The membership of an automobile or travel club does not constitute a qualified group subject to this paragraph.

10. Failure by an insured under the policy to comply with the cooperation or subrogation clause of the policy, subject to reasonable rules established by the Commissioner.

11. Written request by the producer of record not to renew the policy. The producer's request shall include a certification that the policy has been replaced with like coverage at approved rates in the voluntary market with an admitted insurer and shall specify the name of the replacing insurer. The producer's request shall also certify that the insured has been informed in writing of his or her right to renewal and has agreed in writing to the

nonrenewal because the producer has obtained comparable coverage with another insurer. The producer's request not to renew the policy shall be submitted to the insurer not less than 90 days prior to the expiration date of the policy and a copy thereof shall be simultaneously sent by the producer to the named insured.

i. Upon receipt of such request from the producer, the transferor carrier shall advise the insured in writing of his or her right to renewal in the same company before obtaining the insured's consent to transfer and also of the insured's right to renew the policy if he or she is canceled by the new insurer for reasons other than nonpayment of premium or suspension or revocation of the registration or driver's license. Exhibit A appended to this subchapter is approved for this purpose. A nonrenewal based on such request shall be invalid and the original company shall renew the policy at the request of the insured through an active agent and/or broker, or directly if the replacement policy is cancelled by the new carrier for any reason other than the reasons allowed for cancellation by N.J.S.A. 17:29C-7 (nonpayment of premium or suspension or revocation of registration or driver's license).

ii. Failure by a terminated agent to request renewal during the period of nine months from the effective date of termination as provided in N.J.S.A. 17:22-6.14(a) shall be construed as request not to renew in the context of this subchapter. In such event, the insurer shall in writing advise the insured of the status of the agent and that the agent's failure to request renewal denotes that replacement coverage as specified in 11 and 11i above has been obtained. The written notice shall also set forth the insured's right to renewal in the same company as set

forth in 11i. above. Exhibit B appended to this subchapter is approved for this purpose. The insurer's notice shall be sent to the insured not less than 60 days prior to the expiration date of the policy.

iii. Insurance companies and producers shall maintain copies of all correspondence required pursuant to 11, 11i. and 11ii. above for a period of three years.

iv. Notices to insureds set forth in Exhibits A and B shall be sent by certified mail or by regular mail, if at the time of such mailing the insurer has obtained from the Post Office Department a date stamped proof of mailing showing the name and address of the insured. The insurer shall also maintain documentation of the mailing.

(b) An insurer may issue notice of nonrenewal with respect to comprehensive physical damage coverage, including towing and labor coverage, if the insurer, during the 12-month period ended 90 days prior to the expiration of the current policy, has paid under such coverage claims each of which involve a loss payment by the insurer of at least \$100.00, as specified in paragraphs 1 and 2 below:

1. Four or more such claims if there is one car in the household or six or more such claims if there are at least two cars in the household.

2. For any policy which covers more than one car, an insurer may nonrenew comprehensive physical damage coverage, including towing and labor coverage for one of the covered cars, if that single car has four or more claims.

(c) An insurer may issue notice of nonrenewal with respect to towing and labor coverage if the insurer, during the 12-month period ended 90 days prior to the expiration of the current policy, has paid claims under such coverage as specified in 1 below:

1. Four or more such claims if there is one car in the household or six or more claims if there are at least two cars in the household.

(d) Except as provided a N.J.A.C. 11:3-8.4, any refusal to renew a policy or coverage, as applicable, which is not based upon the standards set forth in (a) through (c) above shall be submitted to the Commissioner of Insurance for review no later than 120 days prior to the expiration of the policy. The Commissioner shall, in writing, acknowledge receipt of any refusal to renew submitted pursuant to this subsection. The Commissioner shall, within 45 days of receipt, either disapprove or authorize issuance of any nonrenewal submitted by an insurer for review and acknowledged by the Commissioner pursuant to this subsection. If the Commissioner shall fail to either disapprove or authorize issuance of the nonrenewal within such 45-day period, issuance of the nonrenewal shall be deemed to be authorized.

N.J.A.C. 11:3-8.4 Additional nonrenewals based on underwriting guidelines

(a) An insurer may issue notice of nonrenewal based upon a failure to meet current underwriting

standards as specified in such insurer's underwriting guidelines provided that such nonrenewals may be issued only with respect to a policy:

1. Issued by the insurer to any policyholder who was cancelled pursuant to N.J.S.A. 17:29C-7 or non-renewed pursuant to this subchapter; or

2. Issued by the insurer to any policyholder who was last insured through a statutorily mandated residual market insurance mechanism; or

3. Issued by the insurer to any policyholder who is a first-time applicant for automobile coverage.

- i. For the purposes of this section, the term "first-time applicant" shall mean a person seeking automobile insurance for the first time, including a child applying for a policy in his or her own name after being on their parent's policy.

(b) Pursuant to the provisions of N.J.S.A. 17:22-6.14a1., an insurer's underwriting guidelines shall not be arbitrary, capricious or unfairly discriminatory.

1. Nonrenewals based upon one or more of the following reasons are specifically prohibited:

- i. The race, religion, nationality or ethnic group of an insured;

- ii. Solely upon the lawful occupation or profession of an insured, except that this provision shall not apply to any insurer, agent, or broker which limits its market to one lawful occupation or profession, or to several related lawful occupations or professions;

iii. The principal location of the insured motor vehicle, unless such decision is for a business purpose which is not a mere pretext for unfair discrimination. The insurer shall state the business purpose for such non-renewal and provide the Department with documentation of such purpose on request;

iv. Solely upon the age, sex or marital status of an insured, except that this subparagraph shall not prohibit rating differentials based upon age, sex or marital status;

v. The insured previously obtained insurance coverage through a residual market insurance mechanism;

vi. Another insurer previously declined to insure the insured or terminated an existing policy of the insured.

(c) When policies are written subject to nonrenewal pursuant to this section, the company shall document that the insured is a first time applicant, was cancelled pursuant to N.J.S.A. 17:29C-7 or nonrenewed pursuant to this subchapter or was last insured through a statutorily mandated residual market insurance mechanism. Insurance companies shall maintain copies of such documentation for a period of not less than five years. Such documentation shall be available to the Department on request.

(d) Issuance of a notice of nonrenewal pursuant to this section shall be limited to a period of three years from the date as of which the policy becomes effective after first issuance.

NEW JERSEY
AUTOMOBILE FULL INSURANCE
UNDERWRITING ASSOCIATION
PLAN OF OPERATION

February 7, 1984

ARTICLE V

FINANCIAL

* * *

2. The Association shall derive its income from the following sources for the payment of expenses, losses, loss adjustment expenses, and the provision of adequate, actuarially sound reserves for unpaid losses and loss adjustment expenses, including incurred but not reported losses and not reported loss adjustment expenses, in connection with Association business: (1) net premiums earned; (2) income generated from any Association accident surcharge system permitted or required by law; (3) that percentage of surcharges collected by the Division of Motor Vehicles and deposited with the Association pursuant to subsection b. of section 6 of the "New Jersey Automobile Insurance Reform Act of 1982", and that collected and retained by the Association pursuant to subsection c. of said section 6; (4) income collected as the Residual Market Equalization Charge by members of the Association and by the Association; and (5) income from investment of moneys collected.

* * *

OPERATING PRINCIPLES

PART I – GENERAL

Unless specifically identified otherwise, the Sections of these Operating Principles apply to all automobile coverages.

* * *

SECTION 6: ACTUARIAL

- A. Reserves – The Board shall appoint an Actuarial Committee which shall recommend the methods and standards for the establishment of adequate, actuarially sound reserves for unpaid losses and loss adjustment expense, including provision for incurred but not reported losses and loss adjustment expenses. Such methods and standards shall be reviewed at least annually by the Actuarial Committee and a report on the results, and any suggested changes or amendments to the methods and standards shall be made to the Board.
- B. Report to Commissioner – At least annually, the Board shall file its experience with the Commissioner. This experience shall include the projected income, expenses, losses and reserve requirements of the Association for the ensuing year, any adjustment in previously established reserves for unpaid losses and loss adjustment expenses necessary to make such reserves adequate and actuarially sound, and the initial filing shall include the experience of the automobile insurance plan established pursuant to P.L.1970, c.215 (C.17:29D-1). The Board shall include in its filing with the Commissioner a computation of

the residual market equalization charge (hereafter referred to as "RMEC") per insured vehicle.

The Board shall also include in its filing with the Commissioner a review of the previous year's experience, setting forth the income, losses, loss adjustment expenses, and reserve requirements, including any adjustment in previously established reserves for unpaid losses and loss adjustment expenses necessary to make such reserves adequate and actuarially sound, and expenses of the Association during the previous year. If a profit is found by the Commissioner to have been realized, such amount shall reduce the RMEC levied on policyholders. If a loss is found by the Commissioner to have occurred, such amount shall increase the RMEC levied on policyholders.

Both the filing for the ensuing year and for the previous year shall be in a form established by the Board.

* * *

SECTION 7: COLLECTION AND DISBURSEMENT OF FUNDS

- A. Income – The Association shall derive its income from the following sources for the payment of expenses, losses and loss adjustment expenses, and the provision of adequate, actuarially sound reserves for unpaid losses and loss adjustment expenses, including incurred but not reported losses, in connection with Association business:
1. Net premiums earned;
 2. Income generated from any Association accident surcharge system permitted or required by laws;

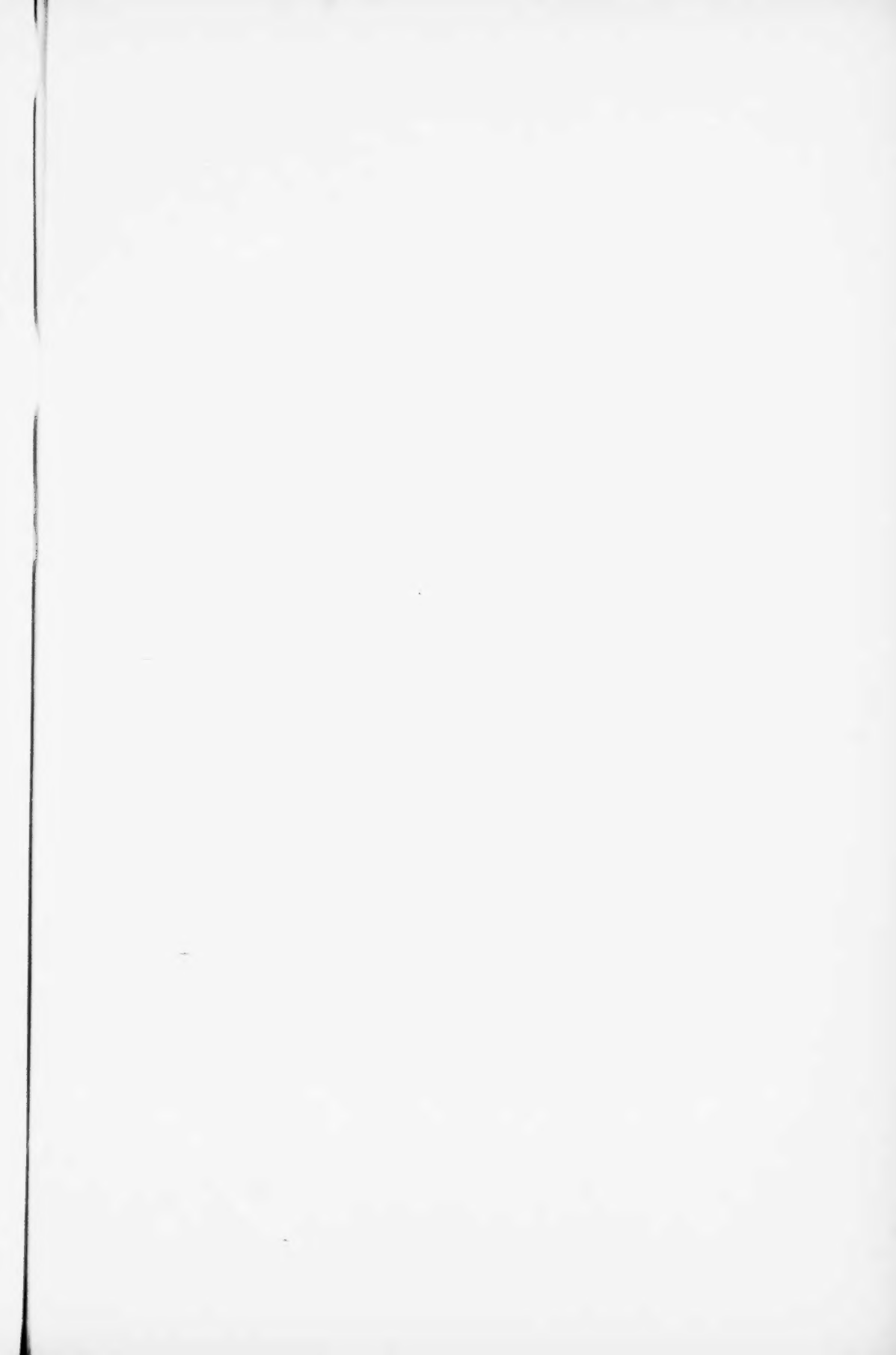
3. That percentage of surcharges collected by the Division of Motor Vehicles and deposited with the Association;
 4. Income earned as the RMEC; and
 5. Income from investment of moneys collected.
- B. Accounts – The Board shall open in the name of the Association such bank account or accounts as it deems necessary.
- C. RMEC Collection – Premiums received on voluntary business by member companies as RMEC on behalf of the Association, net of commissions paid shall on a monthly basis be certified to by the member company and shall be transferred to the Association in accordance with the Rules of Practice.

The RMEC shall be collected following the effective date of its approval by the Commissioner, by each member company from its policyholders, exclusive of principal operators 65 years of age or older, on a uniform net direct car year of liability exposure basis and a net direct car year of physical damage exposure basis. Member companies shall, 15 days prior to the date of the implementation of the revised RMEC, make an informational filing with the Commissioner, documenting compliance with the established method of distributing such RMEC.

- D. Investments – Investments for the Association shall be managed by an investment committee appointed by the Board. Daily cash flow shall be managed by depository banks under cash management contracts. Standards for investments shall be those applicable to property and casualty insurance companies in New Jersey.

- E. Disbursements – Disbursements made on Association business shall be disbursed by the Servicing Carriers or the Association in accordance with the Rules of Practice. Servicing Carriers, as agents of the Association, shall have no liability for claims, or for policies written by the Association.
- F. Premium Collection by Servicing Carriers – All premiums (including RMEC) received by Servicing Carriers on behalf of the Association shall be handled in accordance with the Rules of Practice.
- G. Servicing Carrier Audits – The books of account of Servicing Carriers as they relate to Association business shall be audited with a frequency and in the manner designated by the Board. The auditors will make their report directly to the Board. Costs for the audit, exclusive of ordinary expenses incurred by the Servicing Carriers to support the audit, will be borne by the Association.

* * *



DEC 17 1991

OFFICE OF THE CLERK

In The
Supreme Court of the United States

October Term, 1991

ALLSTATE INSURANCE COMPANY,
an Illinois Corporation,

Petitioner,

v.

SAMUEL F. FORTUNATO,
Commissioner of Insurance of
The State of New Jersey,

Respondent.

Petition For A Writ Of Certiorari To The
Appellate Division Of The Superior
Court Of The State Of New Jersey

APPENDIX, VOLUME II

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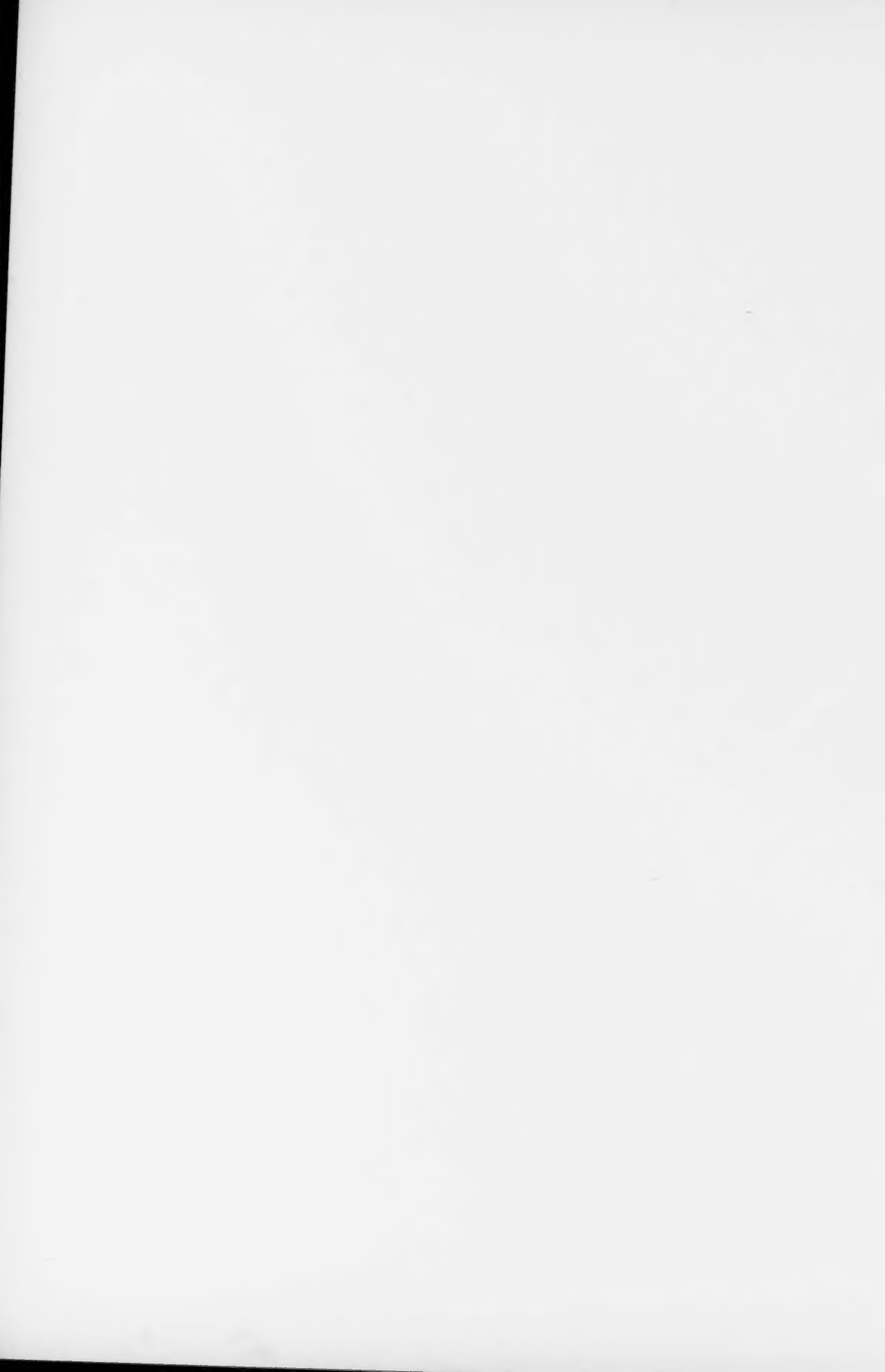


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APPENDIX 8

February 8, 1991

BY HAND

The Honorable Samuel F. Fortunato
Commissioner of Insurance
New Jersey Department of Insurance
20 West State Street
CN 325
Trenton, New Jersey 08625-0325

Re: Request for Stay of January 24, 1991 Depopulation Order

Dear Commissioner Fortunato:

Please accept this letter, in lieu of a more formal brief, in support of the application of Allstate Insurance Company ("Allstate") for a stay pending appeal from the order you issued on January 24, 1991 assigning exposures to Allstate pursuant to the Voluntary Market Program. We have appended a copy of the Order, which Allstate received on January 29, as Exhibit 3 ("Depopulation Order") in the Affidavit and Exhibit Appendix submitted herewith.

Allstate has now filed a notice of appeal in the Appellate Division, with a request that the appeal be expedited. Pursuant to R. 2:9-7, Allstate asks that you stay the Depopulation Order pending disposition of that appeal or until you have acted upon pending requests by Allstate for increases (either interim or permanent) in its automobile insurance rates.¹

¹ The rate relief currently requested by the Market Transition Facility ("MTF") is not adequate, standing alone, to

(Continued on following page)

Introduction

The Depopulation Order has numerous legal deficiencies on its face, some of which will be discussed below. But its most important flaw is its devastating and unconstitutional impact on Allstate if Allstate is required to comply without a sufficient adjustment to Allstate's rates and/or to the MTF rates Allstate would be permitted to charge for the policies issued pursuant to the required offers. Allstate's existing rates are inadequate even to support the costs of providing automobile insurance for its existing policyholders. Yet the Depopulation Order seeks to compel Allstate to issue over 32,000 additional policies at rates which are grossly inadequate to cover the costs of providing that insurance.² Because Allstate's present rates are inadequate for its existing business, that business cannot support the massive losses which would be suffered in connection with the business the Depopulation Order would compel Allstate to write.

(Continued from previous page)

prevent irreparable harm to Allstate; nor is less than the entire interim relief sought by Allstate. However, the requested stay could be reevaluated in light of any relief provided and any findings made in ruling on any of the pending rate requests.

² At present MTF rates, which are somewhat higher than Allstate rates, Allstate estimates an average loss of \$634 on each car insured under these policies, so that the *additional* loss imposed by the Depopulation Order amounts to over \$20 million (and perhaps as much as \$26 million) annually. (Affidavit of Michael A. LaMonica ("LaMonica Aff."), appended hereto as Exhibit 1, ¶ 3.)

The Depopulation Order would thus effect a taking of Allstate's property without just compensation in violation of the United States and New Jersey constitutions and the insurance laws of New Jersey. Because neither the insurance laws nor the Depopulation Order provide any mechanism for recovery of the losses to be suffered if Allstate were to comply with that Order, Allstate would be irreparably harmed by compliance and the Order should be stayed pending an adjudication of its legality or a decision on Allstate's requests for permanent or interim rate relief.

Statement of Facts

As you know, the Department's 1989 study of automobile insurance profitability showed that automobile insurers operating in New Jersey (and Allstate in particular) had suffered massive operating losses for the period 1976-88.³ For the years 1989-90, both the industry and Allstate suffered further aggregate operating losses.⁴

³ A copy of the 1989 study is appended as Exhibit 4. Allstate's losses are further documented by its Annual Statements and rate filings covering this period, which are incorporated by reference.

⁴ Allstate's more recent net losses are documented in the Direct Testimony of David R. Chernick ("Chernick Testimony"), submitted in the Allstate rate hearing now in progress, a copy of which is appended as Exhibit 5. As a result of these persistent operating deficits, Allstate has received no return for 15 years on the substantial capital which it has exposed to the risks of the New Jersey automobile insurance business and has actually lost roughly \$37 million of that capital. (LaMonica Aff. ¶ 4) Had Allstate been able to realize

(Continued on following page)

Moreover, the losses reflected in that study understated the magnitude of the overall problem of rate inadequacy because they failed to take into account the even more massive operating losses of the JUA, as shown by its various filings (most notably those relating to imposition of RMEC), which are incorporated by reference.

The JUA's rates were so severely inadequate that, even with a subsidy from RMEC's and policy constants (currently totaling \$222 for every insured vehicle in New Jersey),⁵ the JUA incurred a deficit of over \$3 billion. In part, this reflected the JUA's heavy concentration of business in territories where rates were especially inadequate due to territorial rate capping imposed by N.J.S.A. 17:29A-36.⁶ As with all other insurers, the JUA rates in the capped territories were far more severely inadequate than the average for JUA rates.

(Continued from previous page)

the 3.5% operating profit which is presumptively proper under Insurance Department regulations (and Allstate contends that a higher rate is actually required under current conditions), it would have earned a total of \$143 million for that period, a result prevented by the consistent refusal of your predecessors to approve adequate rates. (LaMonica Aff. ¶ 4) Thus, rate inadequacy for this period produced confiscation of approximately \$180 million of Allstate's property.

⁵ With approximately 4,300,000 New Jersey vehicles currently insured, RMEC's and policy constants currently provide a subsidy to the JUA rates of almost \$1 billion annually.

⁶ That statute limits the average rate for any territory to 135% of the filer's statewide average rate when, as Special Deputy Commissioner David Grubb observed in 1989, claims per car in the highest-rated territory ranged from 155% to 306% of the statewide average (depending on which coverage was considered). Grubb, *Solving the Auto Insurance Crisis in New Jersey*, 20. (A copy of this report is appended as Exhibit 11.)

The JUA's rates became those of the MTF, but the MTF will not be entitled to either RMEC's or policy constants after April 1. Fair Automobile Insurance Reform Act of 1990 ("FAIRA"), P.L. 1990, c.8, § 17 (to be codified as N.J.S.A. 17:33B-6). Although the MTF has recently obtained two independent actuarial studies indicating that its rates must increase an average of roughly 60% to cover the costs of insuring its current population, it has filed for an increase averaging only 28%.⁷ By filing for a rate increase substantially less than that necessary to cover the costs of insuring its population, the MTF will impose the remainder of those costs (amounting to hundreds of millions of dollars) on Allstate and other private insurers, which are statutorily obligated to absorb the MTF's losses.⁸ FAIRA, § 88 (to be codified as N.J.S.A.

⁷ Copies of those studies are annexed to the Chernick Testimony as Attachment G. The MTF rate filing is appended hereto as Exhibit 6. The studies show that the indicated increase of roughly 60% would allow the JUA to realize neither a profit nor a loss on the policies to be written in the year beginning April 1, 1991, but would leave voluntary-market insurers to absorb a loss of roughly \$330 million dollars from policies the MTF has written or will write at JUA rates during the period October 1, 1990 through March 31, 1991. Were the MTF to receive no increase at all, it would suffer net losses for its entire two years of underwriting totalling over \$1 billion, all of which would have to be covered by voluntary-market insurers.

⁸ According to a memo to you from one of your deputies (copy appended as Exhibit 7), the MTF has limited its request to 28% in order to avoid subjecting "clean" risks to any increase other than the 9.4% flex-rate increase necessary to cover inflationary cost increases. Thus, the proposed increase does nothing to ameliorate the pre-existing gross inadequacy of MTF rates for such risks.

17:33B-11). Moreover, even were the MTF given the 60% indicated average increase (which it has not requested), the MTF rates for the capped territories would remain totally inadequate to cover the costs of insuring drivers in those territories, and involuntary depopulation assignments are made overwhelmingly from the capped territories.

Even had Allstate's rates been adequate for the risks it insured before FAIRA became law, and Allstate submits they were not, FAIRA imposed massive additional costs which were not provided for in those rates. In particular, the depopulation of the JUA requires Allstate to provide insurance at either its own existing rates or those of the JUA/MTF (but without the billion-dollar annual subsidy to the JUA/MTF rates previously provided by RMEC's and policy constants). Yet even with the subsidy provided by RMEC's and policy constants, the JUA rates (which were higher than Allstate's rates) could not cover the costs of insuring JUA policyholders, ultimately producing a deficit of over \$3 billion. Moreover, by accelerating the depopulation process, FAIRA increased the costs currently imposed by that process.⁹ FAIRA also imposed taxes and surcharges to cover the lion's share of the

⁹ An amendment to the JUA Plan of Operation which you first proposed on October 3, 1990 altered the allocation of depopulation quotas among insurers in a way which retroactively increased Allstate's quota by 24,134 exposures. This retroactive change in the formula substantially increased the costs imposed on Allstate.

multi-billion dollar JUA deficit and apparently forbade insurers to recover those taxes and surcharges from policyholders, although you now take the position that they may be recoverable through rate filings in certain circumstances.

Allstate has pending two rate filings (copies appended as Exhibits 12 and 13) which both document the inadequacy of its rates to absorb the enormous extra costs imposed by FAIRA and seek the increases necessary to support those costs. Both are now the subject of what seem likely to be protracted proceedings before permanent relief can be provided. Accordingly, Allstate has filed requests (copies appended as Exhibits 8 and 9) that it be permitted to implement the proposed increases on an interim basis, with the proceeds to be escrowed for distribution in accordance with the ultimate findings in those proceedings. Only if full rate relief (on at least an interim basis) is provided could Allstate's rates be even close to adequate to support the costs of depopulation assignments and the other FAIRA costs.¹⁰

Absent a rate increase, Allstate anticipates an automobile insurance operating loss for policies written in 1991 of 35% of the premiums earned, an amount estimated at \$111,000,000. (LaMonica Aff. ¶ 5) Of this loss, over \$20,000,000 would be produced by compliance with the Depopulation Order. (LaMonica Aff. ¶ 3) Indeed,

¹⁰ For reasons explained in the Chernick Testimony, developments since Allstate made its rate filings indicate that the costs imposed by FAIRA will be even greater than Allstate anticipated at the time it made those filings, so that the increases requested would not in fact be sufficient to support the FAIRA costs. Allstate does not seek any relief at the present time based on the additional costs not anticipated by its pending filings.

even were one to consider all of Allstate's insurance business in New Jersey, rather than just its automobile insurance business, Allstate anticipates a substantial operating loss for 1991 absent automobile insurance rate increases.¹¹ Thus, forced issuance of policies pursuant to the Depopulation Order without first providing adequate rate relief is a naked and uncompensated transfer of Allstate's property to those it is required to insure, in violation of the New Jersey insurance laws and the constitutions of the United States and New Jersey.¹²

In light of FAIRA's apparent prohibition on recovery of the taxes and assessments it imposed, Allstate acted diligently by applying for rate relief relating to those taxes and assessments in August, promptly after you announced the position that they might be recoverable in

¹¹ (LaMonica Aff. ¶ 6) Allstate does not believe that it is proper to consider other lines in pricing automobile insurance and provides this information solely to show that it would make no difference here even were that proper.

¹² Allstate is not even free to avoid this appropriation of its assets by ceasing to write automobile insurance or even by withdrawing entirely from New Jersey. You have adopted a policy of requiring any insurer seeking to withdraw from the New Jersey automobile insurance market to continue writing automobile insurance for several years and to substantially expand that business and increase its losses by accepting involuntary assignments of inadequately rated JUA/MTF business. *In Re Plan of Orderly Withdrawal from New Jersey of Twin City Fire Insurance Co.*, No. A90-151 (N.J. Ins. Dept. Aug. 14, 1990) (copy appended as Exhibit 10). Thus, Allstate has been conscripted to provide automobile insurance and is unable to escape from the burden of confiscatory rates.

some circumstances. (LaMonica Aff. ¶ 7) You have also indicated, in the litigation relating to that filing, that no action could have been taken on such a filing, even had it been made earlier, because you had not yet developed the standards applicable to such filings.

Allstate also acted diligently in making its October filing promptly after it became possible to estimate the rate levels to be required in light of FAIRA and related developments, including the retroactive change in the formula for allocating depopulation obligations. (LaMonica Aff. ¶ 7) That filing was made in time to have permitted action by you, at least on an interim basis, prior to issuance of depopulation assignments.

The Depopulation Order heaps upon insurers enormous losses from the JUA (aggravated by the removal of the billion dollar annual subsidy formerly provided by RMEC's and policy constants). Even with the RMEC's and policy constants, the JUA built a multi-billion dollar deficit in just seven years because of its gargantuan rate inadequacy. The Depopulation Order exacerbates the burden on insurers because it does not merely make assignments from a representative cross-section of the JUA. Rather, it makes assignments preferentially from rating territories with the lowest percentages of vehicles insured in the voluntary market, a disturbed assignment method nowhere authorized by the statute. In general, these territories have low voluntary market coverage precisely because the territorial rate capping imposed by N.J.S.A. 17:29A-36 renders the rates for those territories systematically inadequate.

By assigning insureds overwhelmingly from these territories, the Depopulation Order disproportionately assigns Allstate insureds likely to produce the highest net losses when the rates Allstate is permitted to charge those insureds are compared with the costs likely to be incurred in insuring them. This punitive method of making depopulation assignments from the most severely under-priced insureds in the JUA instead of from an average segment of its population is one of the increased FAIRA costs which Allstate did not anticipate even at the time it made its October rate filing. This change nearly tripled the previously estimated costs associated with the assignments which are made by the Depopulation Order. (Chernick Testimony 12-113)

As explained below, Allstate also contends that the Depopulation Order is facially flawed in a number of other respects. Specifically, Allstate contends that (1) the Depopulation Order is contrary to FAIRA and to the JUA Plan of Depopulation insofar as it purports to require Allstate to offer insurance to those who are not eligible persons entitled to insurance outside the assigned risk plan or the MTF; (2) the Order is contrary to law insofar as it purports to forbid Allstate to non-renew six-month policies which it has a statutory right to non-renew and insofar as it prohibits implementation at the time six-month policies are renewed of rate increases approved during the life of those policies; (3) the Depopulation Order exceeds your statutory authority by requiring Allstate to make offers to 25% more JUA insureds than its depopulation shortfall, even if it has already written enough policies to cover that shortfall; and (4) the Depopulation Order is contrary to law insofar as it

requires Allstate to write the assigned policies through the insureds' former JUA producers.

The need for a stay does not arise solely from the substantive defects of the Depopulation Order, for that Order also sets an extremely burdensome schedule. The Order requires Allstate to begin making offers of insurance on March 1 for policy periods to begin April 1 and thereafter. Even were there no other problems with the Order, this creates enormous administrative difficulties.

To begin with, Allstate did not even receive the Depopulation Order until January 29. Further, the Depopulation Order does not contemplate that Allstate will receive information regarding its actual assignments until at least February 14, and perhaps not until much later. *See* Mandatory Depopulation Assignment Plan ("Assignment Plan"), attached to and incorporated in Depopulation Order, ¶ 19.

Moreover, it will be extremely difficult for Allstate, within 30 days of its January 29 receipt of the Depopulation Order, to analyze data regarding Allstate's ability to make offers to its insureds, design a system to collate that data, program and format that data onto its computers, test the accuracy of the programming and produce finished offers and related materials. (Affidavit of Douglas W. Reynolds, appended hereto as Exhibit 2, ¶ 6) This problem is exacerbated by the fact that Equifax, which is to provide Allstate with much of the necessary information to complete its offer requirements, has produced a test tape as to which much key information is either missing or seemingly inaccurate. *Id.* ¶ 7. Finally, the Order does not give Allstate sufficient time to develop

adequate completed coverage selection forms, to negotiate contracts with adequately trained producers with whom it is being forced to deal or to create a compliance system that will ensure the development of accurate policyholder information in the future. *Id.* ¶¶ 8-10.

Argument

Under New Jersey law, a stay or injunction maintaining the status quo between the parties pending determination of litigation on the merits of a dispute should be ordered if the following criteria are met:

1. the subject matter of the controversy will otherwise substantially change during the pendency of the litigation, thus causing irreparable harm to the moving party;
2. the harm or loss to the opposing party will be minimal; and
3. a substantial question as to the merits has been raised, creating a reasonable probability of success on the merits.

See, e.g., Crowe v. DeGioia, 90 N.J. 126, 132-34, 447 A.2d 173, 176-77 (1982); *Naylor v. Harkins*, 11 N.J. 435, 446, 94 A.2d 824, 828 (1952); *Christiansen v. Local 680 of Milkdrivers*, 127 N.J. Eq. 215, 219-20, 12 A.2d 170, 172 (1939).

Imposition of a stay is particularly appropriate where, in the absence of such relief, the status quo will irreparably change. *See, e.g., Naylor v. Harkins, supra*, 11 N.J. at 446; *Christiansen v. Local 680 of Milkdrivers, supra*, 127 N.J. Eq. at 219. Mere doubt as to the validity of a claim is not an adequate basis upon which to deny a stay. *See, e.g., Crowe v. DeGioia, supra*, 90 N.J. at 133.

1. Irreparable Harm to Allstate Absent a Stay.

The Depopulation Order would, if Allstate is correct, produce irreparable harm in several ways. The first of these is that, without adequate rates, the Order would confiscate Allstate's assets each time it forced Allstate to issue a policy. If, pursuant to the Depopulation Order, Allstate is forced to issue policies at current rates (either its own or those of the MTF), it will be unable to alter those rates for one year after the policy's inception. Assignment Plan, ¶ 21. Allstate also could never recover the losses suffered pursuant to those rates in future rates. *Petition of Elizabethtown Water Co.*, 107 N.J. 440, 453-55, 527 A.2d 354, 363-64 (1987). Thus, issuance of policies at inadequate rates necessarily causes irrecoverable losses, thereby effecting a blatant and unconstitutional seizure of Allstate's assets.

A second way in which the Depopulation Order causes irreparable harm relates to the number and identity of those Allstate must offer to insure. Some of these are statutorily ineligible to procure insurance in the voluntary market because they present too high a risk to be insurable in that market or are similarly ineligible for involuntary assignments under your own depopulation plan. See FAIRA, § 25; New Jersey Automobile Full Insurance Underwriting Association, Plan of Operation ("JUA Plan"), Operating Principles, Section 13, ¶2. Others, while eligible for voluntary-market insurance, are systematically drawn from territories whose rates are the most inadequate and in numbers which Allstate contends far exceed any proper depopulation quota. Put differently, while FAIRA requires only a general JUA depopulation,

the Order goes much further in requiring a specific depopulation by territories.

If Allstate is forced to insure ineligible insureds, or excessive numbers of the most grossly underpriced insureds, it will be irreparably injured because it will be unable to refuse renewal to such insureds except in the most narrowly limited of circumstances. See N.J.S.A. 39:6A-3, 17:29C-7.1; N.J.A.C. § 11:8.3-8.4. Accordingly, in the absence of a stay, Allstate will be unable to take full advantage of any relief the Appellate Division might ultimately grant on the merits.

Nor, absent a stay, could Allstate avoid harm by refusing to comply with the Depopulation Order, for that would subject it to heavy penalties, at least if the Order is found valid.¹³ It is fundamentally unfair to subject a business to severe penalties for failure to comply with a debatable administrative order which it cannot effectively challenge except by non-compliance. In *Re Kimber Petroleum Co.*, 110 N.J. 69, 539 A.2d 1181 (1988). Thus, a stay is appropriate where, as here, the doubtful validity of the order threatens irreparable harm regardless of whether the party subject to the order complies or resists.

¹³ If the Order is unconstitutional or otherwise invalid, its enforcement may properly be enjoined. *Ex Parte Young*, 209 U.S. 123 (1908); *Guarantee National Ins. Co. v. Gates*, 916 F.2d 508 (9th Cir. 1990). Imposition of penalties would similarly be improper in such a case.

2. Absence of any Irreparable Harm Resulting From a Stay.

In contrast to the irreparable harm that will be suffered by Allstate if the Depopulation Order is not stayed, there will be *no harm* if a stay is granted. A stay will simply maintain the status quo for the brief period it will take the Appellate Division to consider the merits of Allstate's appeal or for you to act (at least on an interim basis) on Allstate's rate applications.

No New Jersey insured will be forced to go without coverage if a stay is granted. Rather, the insureds assigned to Allstate will continue to be insured by the MTF. And the Department will always be able to transfer those insureds to Allstate if the Depopulation Order is eventually judicially affirmed.

Consequently, any balancing of the harms weighs heavily in favor of Allstate. That is particularly true since, in the absence of a stay, Allstate will be forced to make offers to its assigned insureds beginning March 1, 1991 – before any appeal from the Depopulation Order can be decided.

3. Allstate's Likelihood of Success on the Merits.

a. Unconstitutional Confiscation

The due process clauses of the United States and New Jersey Constitutions require that New Jersey allow businesses the opportunity to earn a fair rate of return on their activities in the State. *See Duquesne Light Co. v. Barasch*, 488 U.S. 299, 310 (1989); *Helmsley v. Borough of Fort Lee*, 78 N.J. 200, 223, 394 A.2d 65, 70 (1978), appeal

dismissed for want of a substantial federal question, 440 U.S. 978 (1979). This means that regulated rates must be sufficient not only to cover costs and expenses, but also to yield a profit "sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital." *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944) (citations omitted). "[T]he return should be one which is commensurate with returns on investments in other enterprises having comparable risks." *Hutton Park Gardens v. West Orange Town Council*, 68 N.J. 543, 570, 350 A.2d 1, 14-15 (1975). Even apart from constitutional considerations, the legislature has directed that insurers be permitted a fair rate of return. N.J.S.A. 17:29A-4; FAIRA, § 2(g). To force insurers to suffer massive and unrecoverable losses, as the Depopulation Order would do here, is thus to accomplish an unconstitutional and unlawful confiscation of property.

b. Insurance of Ineligible Persons

FAIRA, among other things, establishes a framework for the placement of individuals previously insured by the JUA into the voluntary insurance market or the MTF. N.J.S.A. 17:30E-14. The MTF itself is to insure successively smaller fractions of the market, with its insureds also being moved progressively into the voluntary market, until the MTF insures no more than 10% of all New Jersey vehicles. N.J.S.A. 17:29D-1. At that point, an Assigned Risk Plan is to take over the function of providing insurance to those not insured in the voluntary market. *Id.* However, FAIRA makes it clear that only

certain categories of JUA insureds, known as "eligible persons," are intended to be insured in the voluntary market. FAIRA, § 25 (to be codified as N.J.S.A. 17:33B-13). Others are to be insured through the Assigned Risk Plan once MTF depopulation is complete. Since the whole purpose of depopulation is to move into the voluntary market those insureds who ought not to be relegated to the involuntary market, it would be contrary to the statutory scheme for those who are not eligible persons to be removed from the MTF by assignment to voluntary market insurers.

Eligible persons are statutorily defined to exclude several categories of drivers – those who: (1) in the past three years, have committed a motor vehicle offense; (2) have had their driver's license suspended or revoked; (3) in the past five years, have been involved in insurance fraud; (4) within the past two years, have had a policy cancelled for non-payment of premium; (5) have failed to obtain membership in a club or group, membership in which is a uniform prerequisite to insurance coverage; (6) have had an excessive number of vehicle "points" in the past three years; and (7) possess other risk factors to be determined by the Commissioner. *Id.*

Pursuant to statute, the JUA Plan of Operation specifies the mechanism for the contemplated depopulation of the JUA. JUA Plan, Section 13. That plan further limits insureds eligible for the voluntary market to those who have not been convicted of two or more moving violations, not received four or more vehicle "points," and not had one or more at-fault accidents. *Id.* ¶2. If an individual does not meet these criteria, he cannot be assigned to

insurers who have not met their quota of JUA depopulation business. *Id.*

The Depopulation Order ignores the eligibility standards set by the legislature in FAIRA. Instead, it provides that, in meeting the prescribed depopulation quota, Allstate is to be randomly assigned insureds from the JUA pool – regardless of whether those individuals meet either the JUA Plan eligibility standards or those set by FAIRA for insurability in the voluntary market. *See* Assignment Plan, ¶4. Indeed, the Order expressly prohibits Allstate from failing to accept an assignment where the prospective insured has failed to gain membership in a club, membership in which is a precondition to the writing of insurance, even though that is one of the express eligibility standards set forth in FAIRA.¹⁴ Depopulation Order, 5.

New Jersey state agencies, including the Insurance Department, may not issue orders that are substantively inconsistent with the relevant enabling statutes. *See, e.g., Smith v. Director, Division of Taxation*, 108 N.J. 19, 26, 527 A.2d 843, 846 (1987); *Pascucci v. Vagott*, 71 N.J. 40, 49-51, 362 A.2d 566, 571-72 (1976); *In the Matter of Blue Cross & Blue Shield*, 239 N.J. Super. 434, 452, 571 A.2d 985, 994 (App. Div. 1990). Here, the Depopulation Order conflicts on its face with FAIRA, by permitting completely random assignments to Allstate of insureds from the JUA pool – without regard to their eligibility for voluntary market

¹⁴ Allstate has no such membership requirements, but this provision is illustrative of the Depopulation Order's patent conflict with FAIRA.

status. It also conflicts with the terms of the JUA Plan established pursuant to statutory authority.

c. One Year Prohibition of Non-Renewal and of Implementation of Approved Rate Increases.

One purpose of FAIRA is to allow eligible persons to obtain insurance in the voluntary market. The Depopulation Order, however, goes much further. That Order requires Allstate to insure its assignments at the initial rate for a full year, regardless of whether any rate increase has been approved by you during that period. See Depopulation Order, 4-5.

Normally, Allstate, which issues policies on a six-month basis, would be able (and, indeed, required) to renew its voluntary policies during the second six months of a one-year period at any increased rate that may be in force at the time. N.J.S.A. 17:29A-6. By prohibiting Allstate from doing that here, you are forcing Allstate to provide coverage to its JUA assignments on a more favorable basis than to its voluntary market insureds. That is wholly inconsistent with FAIRA, which requires JUA insureds to be treated equally with – not more favorably than – voluntary market insureds. It is also inconsistent with the rate regulatory statutes, which both permit and require insurers to charge the rates in effect at the time the policy is issued.

• Another impermissible inconsistency between the Depopulation Order and the New Jersey insurance statutes is created by the Order's non-renewal limitation. While the relevant statutes allow for non-renewal of insurance policies in certain instances other than for non-

payment of premium (*see* N.J.S.A. 39:6A-3 and 17:29C-7.1), the Depopulation Order arbitrarily limits Allstate's non-renewal rights, for a full year, to *only* situations where there has been non-payment of premium (Depopulation Order, 5). In other words, even if Allstate would have a *statutory right* to terminate a policy, the Order takes away that right. Once more, such an inconsistency between the Depopulation Order and the relevant statutes is legally unsupportable.

d. Excessive Offers Required

Further, the Depopulation Order requires Allstate to make offers to 25% *more* JUA insureds than its quota, *even if it has already insured enough JUA insureds to meet its quota*. Assignment Plan, ¶¶3, 8. Yet, FAIRA requires only that New Jersey insurers accept *up to* their apportionment share of former JUA business; nowhere in that statute is the Commissioner authorized to force insurers to accept *more* than their share. *See* N.J.S.A. 17:30E-14(b), (c). The requirement of 25% more offers than Allstate's quota is fatally inconsistent with the relevant enabling statute.

e. Requirement To Write Through JUA Producers

Moreover, the Depopulation Order requires Allstate to write and service former JUA business through any randomly selected JUA producer who provides such business. *See* Assignment Plan, ¶4. However, FAIRA explicitly provides that the "procedures governing the increase in market volume shall . . . neither prohibit nor require member companies [such as Allstate] to write

association business through association producers of record. . . . " See N.J.S.A. 17:30E-14(i)(3).

The clear import of the relevant enabling statute is that New Jersey insurers are *not* to be required to deal with any particular producer with respect to JUA business. Of course, the entire purpose of the Depopulation Order is to transfer JUA business to Allstate. Accordingly, that Order, in contravention of FAIRA, plainly *requires* Allstate to deal with JUA producers with respect to JUA business.

By requiring Allstate to deal with particular producers, the Order forces Allstate to in effect employ individuals without regard to their background or credibility. Those individuals can hardly be expected to have the type of commitment to Allstate necessary to form a productive working relationship. That is of particular concern to Allstate because its reputation is, in part, determined by the acts of its agents. Moreover, to the extent these JUA producers breach their contracts with Allstate, or commit other wrongs, Allstate will not be able to terminate them without your approval.

Conclusion

For the foregoing reasons, Allstate is entitled to a stay of the Department's Depopulation Order, pending review of that Order by the Appellate Division or a decision (at least on an interim basis) on Allstate's rate applications. As you are aware, the Depopulation Order requires Allstate to begin compliance by March 1, 1991. Accordingly, if no decision is reached on Allstate's stay motion by, at the very latest, the end of business on

February 19, 1991, Allstate will be deprived of its right to present its stay request before the Appellate Division in sufficient time to obtain full relief. Therefore, Allstate respectfully requests a ruling on its motion for a stay herein prior to that date.

Respectfully yours,

/s/ Suzanne M. McSorley
Suzanne M. McSorley

cc: Douglas S. Eakeley

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APPENDIX 9

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Attorneys for Allstate Insurance Company

IN THE MATTER OF THE)	SUPERIOR COURT
ASSIGNMENT OF)	OF NEW JERSEY
EXPOSURES TO)	APPELLATE DIVISION
ALLSTATE INSURANCE)	DOCKET NO.
COMPANY, A MEMBER)	A-2631-90T5F
COMPANY OF THE NEW)	NOTICE OF APPEAL
JERSEY AUTOMOBILE)	
FULL INSURANCE)	On Appeal from:
UNDERWRITING)	Final Order of the
ASSOCIATION AND THE)	Department of
MARKET TRANSITION)	Insurance
FACILITY OF NEW)	FILED
JERSEY, PURSUANT TO)	FEB 8 1991
THE VOLUNTARY)	
MARKET PROGRAM)	
1991-111)	

TO: THE HONORABLE JUDGES OF THE
SUPERIOR COURT OF NEW JERSEY,
APPELLATE DIVISION

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PLEASE TAKE NOTICE that Allstate Insurance Company ("Allstate") appeals to the Superior Court of New Jersey, Appellate Division, from an Order of the Commissioner of Insurance, dated January 24, 1991 ("Order"), which action is a final agency decision pursuant to R. 2:2-3, for the following reasons:

- (1) the Order's requirement that Allstate supply private passenger automobile coverage to any Joint Underwriting Association ("JUA") insured assigned to Allstate, regardless of whether that person is an "eligible person" under the relevant statutory provision P.L. 1990, c. 8, § 25 (to be codified at N.J.S.A. 17:33B-13) is contrary to law;
- (2) the Order's requirement that Allstate write and service policies through any JUA producer is contrary to law (N.J.S.A. 17:30E-14(i)(3));
- (3) the Commissioner has retroactively altered the formula used in determining Allstate's quota requirements for acceptance as voluntary business of JUA insureds, which alteration prejudicially impacts Allstate;
- (4) the Order requires Allstate to make offers to 25% more insureds than its quota, however that quota is calculated;

- (5) the Order impermissibly forces Allstate to accept insurance risks for which the currently authorized New Jersey rates are grossly inadequate;
- (6) the Commissioner may, for a full year with respect to former JUA policyholders assigned to Allstate, limit Allstate's statutory right (*see* N.J.S.A. 39:6A-3 and 17:29C-7.1) of non-renewal;
- (7) the Order impermissibly prevents Allstate from complying with its normal voluntary market practice of renewing automobile insurance policies every six months at the rate level then authorized by New Jersey law;
- (8) the Order is arbitrary and capricious for all of the above reasons and because: (a) the Order requires Allstate to twice undergo the substantial cost of providing the assigned policyholder with a Coverage Selection Form and Buyer's Guide, even though the relevant statute requires only one such provision; (b) the Order takes away Allstate's right to use any of its own voluntary business practices, with respect to assigned policyholders, for a full year; (c) the Order requires Allstate to begin compliance by March 1, 1991, even though such a start-date for compliance is impractical; (d) the Order requires Allstate to pay numerous costs for the servicing and administration of the depopulation plan that are not required by the relevant enabling statutes; and (e) the Order requires Allstate to begin offering coverage to assigned exposures by March 1, 1991,

even though it does not provide for Allstate to receive information regarding its assignments until some point between March 15 and March 20, 1991; and

- (9) the Order violates principles of fundamental fairness.

A copy of the Order appealed from is attached hereto as Exhibit A.

Dated: Princeton, NJ
February 8, 1991

SMITH, STRATTON, WISE,
HEHER & BRENNAN
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Exhibit A

1. Whether the Depopulation Order's requirement that Allstate supply private passenger automobile coverage to any JUA insured assigned to Allstate, regardless of whether that person is an "eligible person" under the

relevant statutory provision, P.L. 1990, c. 8, § 25, (to be codified at N.J.S.A. 17:33B-13), is contrary to law.

2. Whether the Depopulation Order's requirement that Allstate write and service policies through the JUA producer is contrary to law. (N.J.S.A. 17:30E-14(i)(3).)

3. Whether the Commissioner may retroactively alter the formula used in determining Allstate's quota requirements for acceptance as voluntary business of JUA insureds when such alteration prejudicially impacts Allstate.

4. Whether the Commissioner may require Allstate to make offers to 25% more insureds than its quota, however that quota is calculated.

5. Whether the Depopulation Order impermissibly forces Allstate to accept insurance risks for which the currently authorized New Jersey rates are grossly inadequate.

6. Whether the Commissioner may, for a full year with respect to former JUA policyholders assigned to Allstate, limit Allstate's statutory right (*see* N.J.S.A. 39:6A-3 and 17:29C-7.1) of non-renewal.

7. Whether the Depopulation Order impermissibly prevents Allstate from complying with its normal voluntary market practice of renewing automobile insurance policies every six months at the rate level then authorized by New Jersey law.

8. Whether the Commissioner's Depopulation Order is arbitrary and capricious for all of the above reasons and because: (a) the Order requires Allstate to twice undergo the substantial cost of providing the

assigned policyholder with a Coverage Selection Form and Buyer's Guide, even though the relevant statute requires only one such provision; (b) the Order takes away Allstate's right to use any of its own voluntary business practices, with respect to assigned policyholders, for a full year; (c) the Order requires Allstate to begin compliance by March 1, 1991, even though such a start-date for compliance is impractical; (d) the Order requires Allstate to pay numerous costs for the servicing and administration of the depopulation plan that are not required by the relevant enabling statutes; and (e) the Order requires Allstate to begin offering coverage to assigned exposures by March 1, 1991, even though it does not provide for Allstate to receive information regarding its assignments until some point between March 15 and March 20, 1991.

9. Whether the Depopulation Order violates principles of fundamental fairness.

Exhibit B

1. The precise matter in controversy here is not the subject of any other action pending or about to [sic] brought in this court.

Allstate and the Commissioner Samuel F. Fortunato and the Department of Insurance, however, are parties to several pending matters regarding private passenger automobile insurance in the State of New Jersey, including: *Fortunato v. Aetna Casualty & Surety, et al.*, an administrative action in the State of New Jersey, Department of Insurance (filed 2/20/90); *Allstate Insurance Company v. James J. Florio*, Superior Court of New Jersey, Chancery

Division, Docket No. C-90-0118; *State Farm Mutual Automobile Insurance Company and Allstate Insurance Company v. Samuel Fortunato, et al.*, Supreme Court of New Jersey, Docket No. 32,789; *In the Matter of the Commissioner of Insurance's Certification of Amendments to the New Jersey Automobile Full Insurance Underwriting Association Plan of Operation*, Superior Court, Appellate Division, Docket No. A-5514-89T1; *In the Matter of State of New Jersey, Department of Insurance Order Nos. A89-120 and A89-171 and the Adoption of N.J.A.C. 11:3-16 and N.J.A.C. 11:3-18*, Superior Court of New Jersey, Appellate Division, Docket No. A-5324-88T1; *In the Matter of State of New Jersey, Department of Insurance, N.J.A.C. 11:3-20.1, et seq. and N.J.A.C. 11:3-20A.1*, Superior Court of New Jersey, Appellate Division, Docket No. A-1401-89T1; and *Allstate Insurance Company v. Fortunato, et al.*, Superior Court of New Jersey, Chancery Division, Mercer County, Docket No. C90-0189, on cross-motions for leave to appeal to the Appellate Division, Docket No. AM-585-90-T2.

APPENDIX 10

IN THE MATTER OF THE	)	SUPERIOR COURT
ASSIGNMENT OF	)	OF NEW JERSEY
EXPOSURES TO ALLSTATE	)	APPELLATE
INSURANCE COMPANY	)	DIVISION DOCKET
and	)	NO. A-2631-90T5F
)	
IN THE MATTER OF THE	)	SUPERIOR COURT
ASSIGNMENT OF	)	OF NEW JERSEY
EXPOSURES TO THE	)	APPELLATE
AETNA CASUALTY AND	)	DIVISION DOCKET
SURETY COMPANY	)	NO. A-2618-90T5F
and)	
)	
IN THE MATTER OF THE	)	SUPERIOR COURT
ASSIGNMENT OF	)	OF NEW JERSEY
EXPOSURES TO COLONIAL)	APPELLATE
PENN INSURANCE)	DIVISION DOCKET
COMPANY,)	NO. A-2783-90

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* * *

STATEMENT OF FACTS

New Jersey's High Cost and Underfunded Automobile Insurance System

In 1972, an Automobile Insurance Study Commission proposed the No Fault Act, intending to advance a "reparation objective" of providing prompt benefits to all accident victims and a "cost objective" of reducing or stabilizing automobile insurance prices. Automobile Insurance Study Commission, *Report to Governor and the Legislature, Reparation Reform for New Jersey Motorists*, 7 (1971).

To reduce or stabilize automobile insurance prices while providing compensation for all accident victims (including those whose injuries formerly went uncompensated) would have required that the new system balance the two objectives, either by curtailing some tort recoveries or moving cases out of the lawyer-intensive tort system. However, the No-Fault Act substantially increased compensation for medical bills and other economic losses while doing little to reduce the existing costs of the tort system, eliminating only

cases in which the accident victim incurred less than \$200 in medical expenses. Despite this creation of a *more* costly system, the No-Fault Act responded to the public demand for lower insurance premiums by mandating an artificial 15% *reduction* in automobile insurance premiums. *N.J.S.A.* 39:6A-18.

The resulting high-cost system has been a continuing source of public dissatisfaction. There were numerous legislative efforts to "patch up" the system, but they seldom addressed the expensive benefit package at the heart of the problem. Governor Kean made the point in 1988:

The 'no fault' system adopted in 1972 is grossly out of balance. The implicit promise of any 'no fault' system is prompt payment of medical bills without regard to fault in exchange for a significant limitation on frivolous lawsuits for non-economic damages, such as pain and suffering. This system has never been implemented in New Jersey. While we supposedly enacted a 'no fault' system in 1972, this system maintained the old fault system through its adoption of an unrealistically low \$200 monetary obstacle to litigation. The inevitable result was a more expensive system, as we simply placed a costly new layer on the existing fault system.

Governor's Reconsideration and Recommendation Statement to Senate No. 2637 - L. 1988 c. 119.

In the wake of the 1988 amendments, Special Deputy Insurance Commissioner David N. Grubb undertook a further study of the New Jersey automobile insurance system and produced a report entitled *Solving the Auto Insurance Crisis in New Jersey* (the "Grubb Report"). Among his conclusions were the following (ALA 54A-55A):

Auto insurance premiums are high in New Jersey because of the state's high accident frequency (44% higher than the national average) and the state's unbalanced no-fault law. *The law is unbalanced because the lawsuit limitation does not reduce bodily injury liability premiums enough to offset the costs of mandated PIP medical benefits.*

* * *

In 1988, the state adopted a verbal threshold as the standard auto policy, and now has one of the four most effective lawsuit limitations. The verbal threshold will save the typical motorists with the standard policy approximately \$100 per car as compared to the unlimited right to sue. *However, the no-fault law remains unbalanced because New Jersey mandates the most expensive package of no-fault benefits, and the actual cost of these benefits averages about \$200 per car.*

While New Jersey officials have been unwilling to reduce the costs of the no-fault system enough to bring it into balance, they have not been willing to impose the entire cost of that system on the voting public. As Deputy Commissioner Grubb succinctly put it (ALa 56A):

Since 1973, New Jersey has used tight controls on auto rates to avoid paying the actual cost of the state's high accident rate and unbalanced no-fault system. As a result, the voluntary market has been unprofitable, and the residual market (ie., the JUA) has grown to almost half of the state's motorists.

This general point is confirmed by an *Insurance Profitability Report* published by the New Jersey Department of Insurance in November, 1989, which found that (ALa 47A) (emphasis added):

although private passenger auto has been a profitable insurance line nationally, the *industry* generated a 2.8 percent operating loss, or \$521 million, in New Jersey over a 13-year period ending in 1988.

Since 1976, insurers have lost money on private passenger auto in New Jersey in 10 out of 13 years.

* * *

In fact, over the 13-year period, operating losses on auto insurance have been more severe in New Jersey than in any other state.

The Rise and Fall of the JUA

Because the No-Fault Act required all motorists to maintain insurance, some mechanism was necessary to provide insurance to those unable to procure it in the voluntary market.⁴ This was provided by authorizing the Commissioner to organize a plan through which such motorists could be assigned to insurers which would be required to insure them at rates established by the plan. N.J.S.A. 39:6A-2. These rates were largely based on those in the voluntary market, although drivers with accidents and violations could be subject to higher base rates and to the surcharges for the accidents and violations. Beginning in the 1970's, the Commissioner provided some subsidy

⁴ Ordinarily, even relatively high risks can be insurable if the insurer is able to charge a premium adequate to reflect the risk. If the insurer is not able to charge such a rate or the insured is unwilling or unable to pay it, the insurer will usually be unwilling to insure the risk voluntarily.

to the assigned risk rates by directing incorporation into premium rates for all policies (including those in the voluntary market) of certain "policy constants." However, if the rates charged by an insurer, including the policy constant, proved inadequate, the insurer was obliged to absorb the loss.

In light of the high costs of no-fault insurance and the difficulty of obtaining rates which would cover those costs, many drivers who would otherwise have been attractive customers were unable to procure insurance in the voluntary market. This resulted in a very large Assigned Risk Plan. That made writing new voluntary business even less attractive, because writing such policies carried with it an obligation to accept an increased share of the loss-producing assigned-risk business.

To eliminate this obstacle to voluntary writing, the JUA Act abolished the assigned risk plan and created the JUA as a mechanism to insure those unable to procure coverage in the voluntary market. All New Jersey automobile insurers were required to be members of the JUA and some were to act as servicing carriers to issue policies, collect premiums, and handle claims on behalf of the JUA. However, neither members nor servicing carriers were to have any liability under JUA policies. *N.J.S.A. 17:30E-7(b), -7(c), -8(a)*. A declared purpose of the statute was "to require that companies be made whole for losses in excess of regulated rates on all risks not voluntarily written." *N.J.S.A. 17:30E-2*. Thus, the involuntary market was no longer to act as an obstacle to provision of coverage in the voluntary market.

The JUA was to function as an entirely independent insurance company. Because it would have no capital, it was particularly important that its revenues be adequate and that proper reserves be maintained.⁵

The Legislature contemplated that the rates permitted on JUA policies would be similar to those charged in the voluntary market and, so, would not suffice to pay the losses and expenses of those policies. *N.J.S.A.* 17:30E-13. Thus, it provided the JUA with additional sources of revenue. The JUA was to receive the existing policy constants collected on voluntary-market policies and certain Department of Motor Vehicles surcharges collected from those with bad driving records. *N.J.S.A.* 17:30E-8(a); 17:29A-35. The Commissioner was also empowered to impose a residual market equalization charge ("RMEC") to be collected by insurers on every insured vehicle and remitted to the JUA. The RMEC was to be set, in light of the other resources available, to allow the JUA to operate on a no-profit, no-loss basis. *N.J.S.A.* 17:30E-3(o), 8(b).

⁵ Insurers are required by law to maintain financial reserves sufficient to provide the benefits for which they have already collected premiums. In particular, they must maintain reserves for losses which have been incurred but not yet paid. Examples of such losses include destruction or theft of insured property whose value has not yet been determined, insured liabilities of policyholders asserted in lawsuits that have not yet been concluded, and other claims in the process of adjustment. Such losses also include those which have already occurred but have not yet been reported to the insurer, which must be estimated so that proper reserves can be maintained.

The statute also provided for the appointment of a Board of Directors ("JUA Board"), charged with adopting and filing with the Commissioner a Plan of Operation. *N.J.S.A.* 17:30E-6(a). However, the Commissioner was given total power over the operations and policies of the JUA, and had to approve the Plan before it could take effect. *N.J.S.A.* 17:30E-6(b). The Commissioner had authority to propose amendments to the Plan at any time and unilaterally to adopt those amendments if the JUA Board did not. *N.J.S.A.* 17:30E-6(d).

The JUA Plan was to provide, *inter alia*, "methods and standards for the establishment of adequate and actuarially sound reserves for unpaid losses, including provisions for incurred but not reported losses." *N.J.S.A.* 17:30E-6, -7(r). At least annually, the JUA Board was to file a statement of its financial experience with the Commissioner, including "reserve requirements for the association for the ensuing year, [and] any adjustment to previously established reserves for unpaid losses and loss adjustment expenses necessary to make such reserves adequate and actuarially sound." *N.J.S.A.* 17:30E-8(b). Statutory insurance accounting requires that amounts reserved or added to reserves be treated as expenses in calculating profit or loss.

To operate on a no-profit, no-loss basis, the JUA thus required a RMEC on voluntary-market policies sufficient to fund the necessary reserves. The JUA Plan, as approved by the Commissioner, initially required the JUA Board to recommend a RMEC computed on this basis. JUA Plan, Art. V, ¶ 2 & Operating Principles Part I, §§ 6A, 6B (Feb. 7, 1984). (ALa 231A-235A)

By November 8, 1984, the JUA Board – relying on outside consultant actuaries – recognized the JUA was operating at a loss and needed a RMEC to meet its statutory mandate to balance its books. The Board projected a \$200 million deficit for 1984 and, if no RMEC were charged, a nearly \$2 billion deficit for 1990. Accordingly, the Board decided to ask the Commissioner to approve a RMEC for 1985.

Rather than approve a RMEC for 1985 – a gubernatorial election year – the Commissioner mandated that the JUA adopt a cash-flow method of accounting, paying claims arising out of old policies with premiums received under new policies *without* setting aside the reserves necessary to meet the obligations arising under the policies whose premiums were thus diverted. JUA Plan, Operating Principles, Part I, § 7 (May 24, 1985). (ALa 237A-243A) The JUA Board vigorously objected to the Commissioner's proposal and took an appeal from the Commissioner's decision, but the decision was affirmed. *New Jersey Automobile Full Insurance Underwriting Association v. Hazel Frank Gluck*, Appellate Division, Docket No. A-4870-84T1 (June 19, 1988).

Adoption of cash-flow funding for the JUA made an eventual financial disaster virtually inevitable. The JUA was denied revenues adequate to fund the reserves necessary to pay for losses already incurred, thereby creating a deficit in the assets necessary to pay existing claims. On this basis, the JUA could not pay claims on policies already written without writing policies tomorrow, whose premiums could be diverted to pay claims of prior policyholders. Were the JUA to stop writing new policies, claims already incurred could not be paid unless the JUA

were given other revenues equal to that deficit (plus interest to the time the revenues were collected).

The deterioration of the JUA's financial situation caused by the prolonged freeze of its already inadequate rates and the refusal to implement RMEC's ultimately led to a situation where its ability to meet even its cash flow needs (let alone provide adequate reserves) was in jeopardy. In 1988, the Commissioner finally implemented a RMEC.⁶

The Legislature then defined a class of JUA insureds with bad driving records (two or more moving violations or one or more accidents in the preceding three years) and provided that their rates might exceed standard rates in the voluntary market by 10% in 1989, 20% in 1990, 30% in 1991, and 40% in 1992. *N.J.S.A. 17:30E-13(a) to (d)*. JUA insureds not falling into this limited class of bad drivers were still to be insured at standard rates, *id.*, even though, as Deputy Commissioner Grubb noted, (ALa 72A), they have an accident frequency 35% higher than the voluntary-market drivers for whom such rates were

⁶ The Legislature responded by allowing the JUA to defer payment of some claims and to postpone any increase in the RMEC until revenues became inadequate to fund even the reduced cash-flow needs. *N.J.S.A. 17:30E-8.1*. This statute took an interest-free loan from private insurers by permitting deferral for 12 months of payment of property damage subrogation claims, almost all of which would be due to insurers. It also permitted payment over several years, with interest, of certain tort liability claims. The result of this new deferral of funding for existing JUA liabilities was, as usual, to increase the already enormous deficit in the assets available to meet those liabilities, but to temporarily hold down the premiums to be paid by the voters.

designed. Only in 1993 was the JUA to be permitted to charge rates adequate to the risk presented by those it insured. *N.J.S.A. 17:30E-13(e)*.

The 1988 legislation also sought to depopulate the JUA by returning those with better driving records to the voluntary market. *N.J.S.A. 17:30E-14*. This was not to be done by allowing insurers to charge rates which would make such drivers attractive customers, but by compelling insurers to take them whether or not they were attractive.⁷ The Commissioner then determined that drivers eligible for coverage in the voluntary market were those who had not been convicted of two or more moving violations, had not received four or more vehicle "points," and had not had one or more at-fault accidents. JUA Plan, Operating Principles, Section 13, ¶ 2 (April 28, 1989). (ALa 245A)

FAIRA abolished the JUA and made certain provisions for funding its accumulated deficit. The JUA was forbidden to issue or renew any policy after September 30, 1990, so its last policies would expire by September 30, 1991. FAIRA § 16. RMEC's and policy constants were to remain in effect through March 31, 1991 and to continue to be remitted to the JUA. FAIRA § 18. However, neither RMEC's nor policy constants were to be imposed on or after April 1, 1991. FAIRA § 17.

⁷ The Commissioner was to assign quotas for a minimum number of policies to be written by each insurer in the voluntary market, so that 60% of all vehicles would be so insured during the first year following establishment of the quotas, with the percentage rising to 70% in the second year, and 80% in the third year. *N.J.S.A. 17:30E-14*.

Termination of the JUA's ability to write new policies and of all its other usual sources of revenue made it necessary to provide new sources of funds if claims by and against JUA insureds were to be paid. These new funds were to be provided by newly-created New Jersey Automobile Insurance Guaranty Fund ("Auto Guaranty Fund"). FAIRA § 23. The lion's share of this Fund's revenues were to come from insurance companies.

For three years, automobile insurers will be taxed on their premiums (initially at a rate of 5%, but subject to adjustment) in order to yield \$300 million per year. FAIRA §§ 76-77. The Commissioner must take "such action as is necessary to insure that private passenger automobile insurance policyholders shall not pay the tax." FAIRA § 78.

Additionally, for each of the eight years beginning in 1990, the existing New Jersey Property-Liability Insurance Guaranty Association ("PLIGA") is required to make a "loan" of \$160 million to the Auto Guaranty Fund. FAIRA § 74(10). There are no provisions for payment of interest on these "loans." There is no commitment that the "loans" will be paid at any given time or, indeed, at all.

The PLIGA is to obtain the funds to make these "loans" by assessing all property-liability insurers in proportion to their premiums. FAIRA § 74(9) to (10). For 1990, the assessments have amounted to 2.7% of premiums written, amounting to almost \$10 million for All-state alone. (Asa Tab 5F) For other reasons, the PLIGA ordinarily makes similar assessments; insurers are not

permitted to recover them through the ratemaking process. Ordinarily PLIGA assessments instead may be recovered through surcharges on policyholders, but no surcharges may be imposed to recoup the \$160 million assessments for the Auto Guaranty Fund. *N.J.S.A.* 17:30A-16; FAIRA § 75(b).

The Restructuring of the Automobile Insurance Market

FAIRA substantially restructured the New Jersey automobile insurance system. In light of the JUA's cessation of all writing on September 30, 1990, the MTF was created to arrange for the issuance and renewal of policies from October 1, 1990 through September 30, 1992. FAIRA § 88(a)-(c). It was initially to charge the JUA rates in effect on September 30, 1990. FAIRA § 88(c)(2). The losses suffered by the MTF (or, hypothetically, its profits) were to be shared among the insurers doing business in the voluntary market. FAIRA § 88(a). The depopulation of the JUA into an expanded "voluntary" market already in progress was to proceed faster and farther than previously scheduled.⁸

⁸ At least 68% of New Jersey vehicles were to be insured in the voluntary market by October 1, 1990. FAIRA § 20. No more than 29% were to be insured by the MTF after April 1, 1991, no more than 20% after October 1, 1991, no more than 10% after April 1, 1992, and no new policies were to be issued after October 1, 1992. FAIRA § 88(c)(5). As before, insurers in the voluntary market were to be assigned quotas of voluntary-market insurance to be provided to meet these goals. *Id.* If they failed to fulfill these quotas, insureds were to be assigned to them. *Id.*

The new insurance system was structured in part by defining a broad class of "eligible persons" entitled to insurance in the voluntary market. FAIRA §§ 25-26. Such persons were to be insured through a new assigned risk plan (or through the MTF until an assigned risk plan is created), with any losses produced by rate inadequacy falling on the insurers to whom risks are assigned. FAIRA §§ 24, 88. Beginning April 1, 1991, "eligible persons" will have a statutory right to purchase insurance from any licensed insurer, as such insurers will be required to "take all comers" from that broad class. FAIRA § 27(b).

The New Jersey Insurance Ratemaking System

If an insurer's rates are inadequate, New Jersey law does not permit the resulting losses to be recovered through future rate increases. *In Re Elizabethtown Water Co.*, 107 N.J. 440, 449-51, 527 A.2d 354, 359-60 (1987); *In Re Industrial Sand Rates*, 66 N.J. 12, 23, 327 A.2d 427, 433 (1974). Yet all increases require the prior approval of the Commissioner, who has extensive power to delay or deny such increases even if well justified. As Deputy Commissioner Grubb noted, the Commissioner's power to delay or deny rate increases has been freely used to avoid making New Jersey motorists pay the full costs of the expensive automobile accident reparations system ordained by the legislature. (ALa 56)

Since 1944, the New Jersey insurance statutes have directed that rates be made "not unreasonably high or inadequate for the safety and soundness of the insurer, and which do not unfairly discriminate between risks in this State involving essentially the same hazards and

expense elements." N.J.S.A. 17:29A-4. This has consistently been interpreted to require that the premium should be sufficient to cover the costs of providing the particular type of insurance, including a reasonable return on the capital required to support the provision of the insurance. Specifically, New Jersey automobile insurer is entitled, absent a showing that either its business is inefficiently conducted or that a greater return is necessary, to rates which are projected to provide an "operating profit" (which takes account of the insurer's investment income attributable to insurance operations) of 3.5% of the premiums. N.J. Admin. Code 11:3-16.1; see *In Re: Application of Insurance Rating Board*, 63 N.J. 413, 307 A.2d 604 (1973).

To alter its rates, an insurer is required to file proposed amendments with the Commissioner and to obtain his approval. N.J.S.A. 17:29A-14. Before acting upon proposed amendments, the Commissioner could certify the filing for a hearing and is required to do so on request. *Id.*

However, until 1983, there were no limits on the time for the Commissioner to act upon proposed changes to a rating system. *Insurance Co. of North America v. Howell*, 80 N.J. Super. 236, 193 A.2d 386 (App. Div. 1963). Until the Commissioner decided, the insurer ordinarily would not have exhausted its administrative remedies and, so, would be unable to obtain substantive judicial review. After a decision, judicial review of a denial or partial denial of the insurer's application would likely consume many months, if not years. The Commissioner thus possessed almost unreviewable discretion to delay rate increases, no matter how well justified, for protracted periods.

In 1983, the Legislature imposed some time limits on the period the Commissioner may take to act on a rate application. But the Commissioner still has broad power to demand additional information before commencing hearings and there is no limit on the length of such hearings. *N.J.S.A. 17:29A-14c*.

In most lines of insurance, an insurer unable to obtain adequate rates could curtail its writings in the affected market or withdraw entirely. However, the No-Fault Act generally forbids insurers to decline to renew automobile insurance policies without the Commissioner's consent. *N.J.S.A. 39:6A-3; N.J.S.A. 17:29C-7.1*. The Commissioner's consent to non-renewal is granted only in extreme circumstances. *N.J. Admin. Code 11:3-8.3 to 8.4*. The requirement for the Commissioner's consent to non-renewal applies even when an insurer seeks to entirely withdraw from writing automobile insurance or even all insurance in New Jersey. *Sheeran v. Nationwide Ins. Co.*, 80 N.J. 548, 556-57, 404 A.2d 625, 631 (1979). FAIRA expressly prohibits withdrawal from writing automobile insurance except pursuant to a plan of orderly withdrawal approved by the Commissioner. FAIRA § 72.

Because of this, the Commissioner has substantial power to prevent or delay an insurer from curtailing its writings of automobile insurance, or withdrawing from that market, and he may attach onerous conditions to any consent for it to do so. This enormously increases the impact of the Commissioner's virtually unreviewable power to delay or deny rate increases.

In recent years a number of insurers have withdrawn or sought to withdraw from the New Jersey automobile

insurance market, and the Commissioner has consistently attached burdensome conditions to his consent to permit the necessary non-renewals. In light of FAIRA, he has formalized a policy of requiring an insurer desiring to withdraw from writing automobile insurance to cease writing any other type of insurance, but to continue writing automobile insurance (and to expand its writings pursuant to the depopulation process and the take-all-comers requirement) for five years unless it can find another insurer willing to assume its obligations in these regards. *In Re Plan of Orderly Withdrawal from New Jersey of Twin City Fire Insurance Co.*, No. A90-151 (N.J. Ins. Dept. Aug. 14, 1990). Indeed, the withdrawing insurer must cease voluntary writings, so its entire depopulation obligation must be met through involuntary assignments. *Id.*

Capping of Territorial Rate Differentials

Insurance rates vary among different locations. In setting rates for individual insureds, insurers utilize many factors which have been found predictive of the differing levels of risk presented by different insureds. In this way, each insured pays only for the risks he presents and rates can be set which make even higher-risk insureds attractive customers. Among the most important of these predictive factors is the territory in which a vehicle is located, which reflects population density, traffic conditions, repair costs, and other factors which determine the frequency of accidents and the cost levels associated with them.

In 1983, the Legislature altered the ratemaking standard for automobile insurance rates by artificially "capping" the differentials in rates to be charged various classes of insureds. *N.J.S.A. 17:29A-36*. In particular, the base rate for a particular coverage in any given rating territory, exclusive of driving record surcharges and discounts, could not exceed 1.35 times the filer's statewide average base rate for that coverage. *N.J.S.A. 17:29A-36(c)*. Of course, no caps would be necessary but for the fact that cost differentials among territories or classes of insureds in the same territory would dictate rate differentials larger than those permitted by the caps. For example, claims per car in New Jersey's highest rated territory ranged from 155% to 306% (depending upon the coverage involved) of statewide average claims per car. (ALa 73A)

Artificial capping of rate differentials when actuarial data shows cost differentials exceeding the "caps" requires that some insureds be charged prices which do not reflect the full cost of the insurance provided. This resulted in creation of a class of underpriced customers, whom no insurer would voluntarily insure, thereby constricting availability of insurance in the voluntary market. (ALa 74A-75A)

The Historic and Continuing Inadequacy of New Jersey Automobile Insurance Rates and the Pending Rate Proceedings

The Insurance Department's own study showed that automobile insurers operating in New Jersey (and All-state in particular) had suffered massive operating losses for the period 1976-88. For the years 1989-90, both the

industry and Allstate suffered further aggregate operating losses.⁹ Moreover, the losses reflected in that study understated the magnitude of the overall problem of rate inadequacy because they failed to take into account the even more massive operating losses of the JUA.

The JUA's rates were so severely inadequate that, even with a subsidy from RMEC's and policy constants (currently totaling \$222 for every insured vehicle in New Jersey),¹⁰ the JUA incurred a deficit of over \$3 billion. In part, this reflected the JUA's heavy concentration of business in territories where rates were especially inadequate due to territorial rate capping. As with all other insurers, the JUA rates in the capped territories were far more severely inadequate than the average for JUA rates.

The JUA's rates became those of the MTF, but the MTF will not be entitled to either RMEC's or policy constants after April 1. FAIRA § 17. Although the MTF

⁹ As a result of these persistent operating deficits, Allstate has received no return for 15 years on the substantial capital which it has exposed to the risks of the New Jersey automobile insurance business and has actually lost roughly \$37 million of that capital. (ALa 44A, ¶ 4) Had Allstate been able to realize the 3.5% operating profit which is presumptively proper under Insurance Department regulations (and Allstate contends that a higher rate is actually required under current conditions), it would have earned a total of \$143 million for that period, a result prevented by the consistent refusal of Commissioners to approve adequate rates. (ALa 44A, ¶ 4) Thus, rate inadequacy for this period produced confiscation of approximately \$180 million of Allstate's property.

¹⁰ With approximately 4,300,000 New Jersey vehicles currently insured, RMEC's and policy constants currently provide a subsidy to the JUA rates of almost \$1 billion annually.

has recently obtained two independent actuarial studies indicating that its rates must increase an average of roughly 60% to cover the costs of insuring its current population, it has filed for an increase averaging only 28%.¹¹ (ALa 187A-227A; ALa 140A-144A) By filing for a rate increase substantially less than that necessary to cover the costs of insuring its population, the MTF will impose the remainder of those costs (amounting to hundreds of millions of dollars) on Allstate and other private insurers, which are statutorily obligated to absorb the MTF's losses.¹² FAIRA § 88. Moreover, even were the MTF given the 60% indicated average increase (which it has not requested), territorial rate capping assures that the MTF rates for the capped territories would remain totally inadequate to cover the costs of insuring drivers in those territories, and involuntary depopulation assignments are made overwhelmingly from the capped territories.

¹¹ The studies show that the indicated increase of roughly 60% would allow the JUA to realize neither a profit nor a loss on the policies to be written in the year beginning April 1, 1991, but would leave voluntary-market insurers to absorb a loss of roughly \$330 million from policies the MTF has written or will write at JUA rates during the period October 1, 1990 through March 31, 1991. Were the MTF to receive no increase at all, it would suffer net losses for its entire two years of underwriting totalling over \$1 billion, all of which would have to be covered by voluntary-market insurers.

¹² According to a memo to the Commissioner from one of his deputies, the MTF has limited its request to 28% in order to avoid subjecting "clean" risks to any increase other than the 9.4% flex-rate increase necessary to cover inflationary cost increases. (ALa 145A-146A) Thus, the proposed increase does nothing to ameliorate the pre-existing gross inadequacy of MTF rates for such risks.

Even had Allstate's rates been adequate for the risks it insured before FAIRA became law, and Allstate submits they were not, FAIRA imposed massive additional costs which were not provided for in those rates. In addition to the taxes and assessments previously mentioned, the accelerated depopulation of the JUA requires Allstate to provide insurance at either its own existing rates or those of the JUA/MTF. Yet even with the billion-dollar annual subsidy previously provided by RMEC's and policy constants, the JUA rates (which were higher than Allstate's rates) could not cover the costs of insuring JUA policyholders, ultimately producing a deficit of over \$3 billion.

Allstate has pending two rate filings which document the inadequacy of its rates to absorb the enormous extra costs imposed by FAIRA and also seek the increases necessary to support those costs. (Asa Tabs 12, 13) Both are now the subject of what seem likely to be protracted proceedings before permanent relief can be provided. Accordingly, Allstate has filed requests that it be permitted to implement the proposed increases on an interim basis, with the proceeds to be escrowed for distribution in accordance with the ultimate findings in those proceedings. (Asa Tabs 8, 9) Only if full rate relief (on at least an interim basis) is provided could Allstate's rates be even close to adequate to support the costs of depopulation assignments and the other FAIRA costs.¹³

¹³ Developments since Allstate made its rate filings indicate that the costs imposed by FAIRA will be even greater than Allstate anticipated at the time it made those filings, so that the

Absent a rate increase, Allstate anticipates an automobile insurance operating loss for policies written in 1991 of 35% of the premiums earned, an amount estimated at \$111,000,000. (ALa 44A, ¶ 5) Of this loss, over \$20,000,000 would be produced by compliance with the Depopulation Order.¹⁴ (ALa 43A-44A, ¶ 3) Indeed, even were one to consider all of Allstate's insurance business in New Jersey, rather than just its automobile insurance business, Allstate anticipates a substantial operating loss for 1991 absent automobile insurance rate increases. (ALa 44A, ¶ 6) (Allstate does not believe that it is proper to consider other lines in pricing automobile insurance and provides this information solely to show that it would make no difference here even were that proper.)

(Continued from previous page)

increases requested would not in fact be sufficient to support the FAIRA costs. When Allstate made its October rate filing, it did not anticipate that depopulation assignments would be made from the most severely underpriced insureds in the JUA instead of from an average segment of its population. This change nearly tripled the previously estimated costs associated with the assignments which are made by the Depopulation Order. (ALa 159A) Allstate does not seek any relief at the present time based on the additional costs not anticipated by its pending filings.

¹⁴ At present MTF rates, which are somewhat higher than Allstate rates, Allstate estimates that it will suffer an average loss on each assigned exposure of \$634, for a total loss of as much as \$26 million, if it is given the maximum number of assignments (25% in excess of its shortfall in achieving its quota) called for by the Depopulation Order. (ALa 43A-44A, ¶ 3) Once a policy is issued at inadequate rates, Allstate is powerless to increase the rate for that policy, so the loss resulting from the rate inadequacy becomes unavoidable.

The Depopulation Order directs the MTF to assign to Allstate 32,687 exposures (the amount by which Allstate falls short of its retroactively increased depopulation quota) in accordance with the Assignment Plan. (ALa 3) However, the Assignment Plan directs that the number of assignments specified be increased by 25%, ostensibly to cover rejections by those to whom offers of insurance are made. (ALa 9, ¶ 3) But Allstate must continue to make offers pursuant to the Depopulation Order "even when [it] has written sufficient exposures to meet its apportionment share shortfall." (ALa 10A, ¶ 8)

Assignment percentages are computed by territory. Exposures are first assigned from the territory with the smallest percentage of vehicles insured by private insurers, until the remaining JUA/MTF percentage in that territory equals that in the territory with the next lowest private market percentage, and so on until all the necessary assignments are made. (ALa 8A, ¶ 2)

Within each territory, actual assignments are made by selecting insurance producers (agents or brokers) based on the size of their books of business and the shortfall of the particular company. Each selected producer is then assigned to a company, which must make offers of insurance to that producer's existing customers as their respective JUA/MTF policies expire. (ALa 9A-10A, ¶¶ 4-6) *Every* policy is declared eligible for assignment. (ALa 9A, ¶ 4)

While the producers of assigned policies have no right to place new business with the company unless it agrees to accept such business, such producers have the

right to service their assigned policies, including submitting requests (which the insurer is required to honor) for changes in coverage, limits, options, deductibles, or cars. (ALa 16A, ¶ 21; ALa 13A, ¶ 12(b)) The assigned insurer must compensate the producer of an assigned policy and must continue to do so for as long as it insures the risk. (ALa 15A-16A, ¶ 20) It may not require the producer to satisfy any performance standards greater than those of the MTF, so that, for example, it may not require the producer to maintain errors and omissions coverage. (ALa 17A, ¶ 23) It may not terminate or discipline a producer even for violating MTF performance standards, but can only request the MTF to take disciplinary action. (ALa 17A, ¶¶ 24-25)

* * *

II. IN THE FACE OF ALLSTATE'S PRIMA FACIE SHOWING THAT THE DEPOPULATION ORDER WOULD HAVE A CONFISCATORY EFFECT, THE COMMISSIONER MAY NOT COMPEL ALLSTATE TO COMPLY WITH THAT ORDER WITHOUT FIRST CONDUCTING FURTHER PROCEEDINGS.

A. Allstate Has Made a Prima Facie Showing That The Depopulation Order Would Have a Confiscatory Effect On It.

Allstate has shown, and it is virtually admitted, that the rates it is permitted to charge for the business to be assigned are themselves inadequate even to cover the costs of providing that insurance, let alone provide a fair

return on that business.²⁰ Specifically, Allstate has shown that it projects an operating loss exceeding \$20 million annually from issuing assigned policies at MTF rates (and, necessarily, and even larger loss if it used its own, lower rates). This showing is further bolstered by the two actuarial studies obtained by the MTF, an entity whose board members are appointed by public officials, not insurers. FAIRA § 88(b). This showing is further bolstered by the longstanding inadequacy of JUA rates which led the JUA to utter insolvency (even with a \$1 billion annual subsidy which now will cease to exist). Special Deputy Commissioner Haskins has recognized this, at least in part, by recommending a 28% increase in the MTF rates.

Moreover, Allstate's showing is overwhelming when it is remembered that Allstate is not to be assigned merely a representative share of the JUA/MTF business, but is to be given business selected from the most severely underpriced of the JUA's territories, a fact which nearly triples the expected loss. (ALA 159A) Again, the Commissioner essentially admits this point when he argues that his method of selecting the risks to be

²⁰ Allstate is entitled to a fair return on the involuntarily assigned business, standing alone. See *California State Auto Ass'n v. Maloney*, 341 U.S. 105, 108 (1951) (upholding assigned risk statute because "the premiums chargeable could be commensurate with the greater risks of the [assigned] business"); *Sheeran v. Nationwide Ins. Co.*, 80 N.J. 548, 560, 404 A.2d 625, 631 (1979) (insurer forced to continue writing automobile insurance as condition of retaining its license entitled to a reasonable profit on that business). However, it is not necessary to reach that question here because Allstate faces losses on its entire New Jersey automobile insurance business and, indeed, on all of its New Jersey insurance business.

assigned was adopted in order to avoid the need for an "extraordinary increase" in the MTF rates. (Csb 11)

Nor can the loss imposed by the Depopulation Order be supported by profits from Allstate's voluntary automobile insurance business, for Allstate has shown that it is experiencing massive operating losses as a result of the Commissioner's refusal to approve adequate rate increases. This showing is bolstered by the Insurance Department's profitability study, which showed large industry-wide operating losses for the period 1976-88, including losses in 10 out of 13 years. Moreover, the Commissioner would not feel the need to erect ever-higher barriers to withdrawal from the automobile insurance business if automobile insurers could expect to earn profits adequate to attract capital to the business.

Finally, Allstate has shown that, at present rates, any profits it might hope to make in other New Jersey lines of insurance will be completely overwhelmed by its automobile insurance losses, thus producing a large aggregate operating loss on all New Jersey insurance operations of Allstate and its affiliates. Thus, even at this level, there would be no profits to support the losses which would be imposed by the Depopulation Order. By any standard, Allstate has made a prima facie showing that the Order has confiscatory impact.

If Allstate is forced to issue policies pursuant to an inadequate rate structure, it will suffer irreparable harm. To begin with, once a policy is issued at an inadequate rate, Allstate is powerless to alter that rate for the duration of the policy. Each such policy, once issued, will

produce an average loss equal to the deficiency in the applicable rate.

Nor may Allstate recoup any such deficiency in today's rates by attempting to charge higher rates at some time in the future. Rates must be fixed solely with reference to the anticipated costs of the service to be provided in the period to which they will apply; past rate deficiencies may not be used as a basis for future charges higher than otherwise justified. *In Re Elizabethtown Water Co.*, 107 N.J. 440, 449-51, 527 A.2d 354 359-60 (1987); *In Re Industrial Sand Rates*, 66 N.J. 12, 23, 327 A.2d 427, 433 (1974). Consequently, "rates must provide a constitutional return in the [period] in which they are in effect." *Helmsley v. Borough of Fort Lee*, 78 N.J. 200, 230, 394 A.2d 65, 80 (1978) (emphasis added), *app. diss'd*, 440 U.S. 978 (1979).

B. Allstate Is Entitled to the Opportunity to Earn a Fair Rate of Return on Its New Jersey Business.

The power to regulate a business does not include the "power to compel the doing of [regulated] services without reward." *Troy Hills Village v. Township Council*, 68 N.J. 604, 620, 350 A.2d 34, 42 (1975). Nor may such a business be compelled to subsidize the needs of its customers. *Id.*

The United States and New Jersey Constitutions require New Jersey to allow businesses the opportunity to earn a fair rate of return on their activities in the State. *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 310 (1989); *Helmsley v. Borough of Fort Lee*, 78 N.J. 200, 223, 394 A.2d 65, 70 (1978), *app. diss'd*, 440 U.S. 978 (1979). This means that regulated rates must be sufficient not only to cover

costs and expenses, but also to yield a profit "sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital." *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944) (citations omitted). "[T]he return should be one which is commensurate with returns on investments in other enterprises having comparable risks." *Hutton Park Gardens v. West Orange Town Council*, 68 N.J. 543, 570, 350 A.2d 1, 14-15 (1975). Even apart from constitutional considerations, the Legislature has directed that insurers be permitted a fair rate of return. N.J.S.A. 17:29A-4; FAIRA § 2(g); see N.J. Admin. Code 11:3-16.2. To force insurers to suffer massive and unrecoverable losses would thus impermissibly confiscate property.

These standards apply even where the regulated party is free to avoid the confiscatory effect by abandoning the business. *Hutton Park Gardens. supra*, 68 N.J. at 568-69 n.9, 350 A.2d at 14 n.9. But they are especially compelling when, as here, the regulated party is forbidden to abandon the business and has also been conscripted to take on substantial volumes of underpriced new business.

C. Allstate's Showing of Confiscation May Not Be Avoided by Reliance on Past or Future Flex-Rate Increases or the Possibility That Allstate Might File a Non-Standard Rating Plan.

In response to Aetna's motion for a stay, the Commissioner relied on two avenues of rate relief which he claimed Aetna had ignored and which might ameliorate any confiscatory impact. (Csb 18) He alleged that Aetna

was entitled to file for an automatic flex-rate increase of up to 6% now and another such increase (in an as-yet unknown amount) on July 1, 1991. He also alleged that Aetna was entitled to file for a non-standard rate level of up to 35% above its average rate level.

1. Flex-Rate Increases Are Not a General Solution to the Problem of Regulatory Lag.

Allstate has already taken a flex-rate increase, on July 1, 1990, and will not be entitled to another until July 1, 1991. Thus, such an increase can be of no current assistance. More generally, while flex-rate increases do reduce the impact of regulatory lag in processing rate applications, they do not ameliorate the types of rate inadequacy present here.

Flex-Rate increases are designed to avoid delaying rate adjustments necessary to provide for certain increasing costs which could be shown or anticipated without specific examination of the experience of individual companies. *N.J.S.A. 17:29A-44*. Beginning July 1, 1989, insurers were permitted to make annual "flex-rate" increases based on the percentage increase in specified components of the Consumer Price Index, relating to medical services and automobile repairs. Flex-Rate increases were thus designed to provide automatic relief for certain categories of increasing costs, with the result that adequate rates would be less likely to become inadequate with passage of time. However, flex-rate increases could not cure pre-existing rate inadequacy and they make no provision for cost increases resulting from new legislation or other extraordinary events.

Because the problems of rate inadequacy created by the Depopulation Order are the result, not of rising medical and automobile repair costs, but rather of wholesale restructuring of the automobile insurance system, last July's flex-rates could not eliminate those problems. Moreover, next July's increase will merely compensate for rising medical and repair costs which have occurred in the last seven months, and will occur in the next five, without regard to the restructuring of the system. Thus, they too will be unable to compensate for rate inadequacies created by the restructuring. Finally, next July's increase may be delayed by as much as nine months if the Public Advocate objects to it. FAIRA § 36, *amending N.J.S.A. 17:29A-44f.*

2. Non-Standard Rate Plans Offer No Immediate Relief and Only Minimal Ultimate Relief, So They Cannot Avoid the Need for Other Action To Protect Against Rate Inadequacies.

It is now true, as the Commissioner says, that implementation of a non-standard rating plan could provide some additional revenues for Allstate and other insurers.²¹ But a non-standard rating plan must be filed with Commissioner, and must be approved by him before

²¹ Prior to November 26, 1990, it was the Commissioner's policy that no non-standard rating plan could be approved which did not reduce the standard rates sufficiently to offset any revenue from the increased rates. Under that requirement of revenue neutrality, mere filing of a non-standard rate plan could not result in any additional revenues to the filer. That requirement was eliminated by emergency regulations promulgated on November 26, 1990. (ALa 285A, ¶ 3; ALa 286A, ¶ 5)

it can be put into effect. *N.J.S.A.* 17:29A-45. Under FAIRA, such a plan must comply with certain determinations made by the Commissioner. FAIRA § 37. Prior to November 26, 1990, the Commissioner had not approved any method of making such determinations. (ALa 286A, ¶ 4) Before that time, insurers could not even begin to design such a plan.

Moreover, permanent regulations were not adopted until January 25, 1991, the day after the Depopulation Order was entered. While emergency regulations had been promulgated on November 26, 1990, they were necessarily effective only briefly and there could be no advance assurance that the permanent regulations would be the same or even similar. Thus, it was not prudent to expend substantial efforts designing and filing a plan which might not comply with the final regulations. (ALa 286A-287A, ¶ 6)

The final regulations were adopted on the eve of the hearing on Allstate's October 15 rate filing. The personnel who are responsible for designing and filing the non-standard rate plan were and are heavily involved in that hearing and have not yet had sufficient time to also act in response to adoption of the final regulations. However, Allstate will file such a plan by March 1, as required by the regulations. (ALa 287, ¶ 7)

Accordingly, Allstate has not yet had a fair opportunity to file a non-standard rate plan. Moreover, there is no assurance that, had Allstate somehow managed to do so, its plan would have been or would soon be approved. Thus, such a plan cannot and could not fairly be relied

upon as a source of immediate relief or relief at any time in the near future.

Moreover, the relief provided by the filing of a non-standard rating plan would be minimal. Only 15% of drivers can be placed in such a plan. FAIRA § 37. Allstate has made an analysis of various designs it might employ and finds that such a plan might provide revenues amounting to about 6% of standard premiums. (ALa 287A, ¶¶ 8-9) However, implementation of such a plan would also require Allstate to eliminate its existing system of surcharges for accidents and violations, which surcharges amount to roughly 3% of its existing revenues. (ALa 287A-288A, ¶ 10) Thus, implementation of a non-standard rating plan would provide additional revenues roughly equal to a 3% rate increase. (ALa 289A, ¶ 11) While such revenues would be welcome, they would not even approach the levels necessary to prevent a confiscatory impact from the Depopulation Order.

Finally, even a non-standard rating plan would do little to respond to the specific problems of the Depopulation Order. Most drivers in the JUA are there not because they have bad driving records, but simply because insurers are not permitted to charge rates adequate to the risks they present.

D. Current Confiscatory Impact Is Not Justified by the Mere Prospect That Currently Pending Rate Proceedings May Eventually Lead to the Setting of Non-Confiscatory Rates.

Unless the losses suffered on account of currently inadequate rates will be compensated at some future

time, current confiscation cannot be justified on the basis that it will continue only until determination of a final rate or completion of some other proceeding. *Prendergast v. New York Telephone Co.*, 262 U.S. 43 (1923). In *Prendergast*, a telephone company was ordered to reduce its rates pending completion of hearings to set rates. The order was said to be "temporary," but (as is true in New Jersey) no procedure was available to recoup in the future any deficits which might be incurred while the "temporary" order was in effect. The Supreme Court sustained a preliminary injunction staying the rate reduction but requiring the company to refund any charges above the level originally ordered which were later found excessive.

The Court held that the ostensibly temporary character of the order did not

deprive the company of its right to relief at the hands of the court. The orders required the new reduced rates to be put into effect on a given date. They were final legislative acts as to the period during which they should remain in effect pending the final determination; and if the rates prescribed were confiscatory the Company would be deprived of a reasonable return upon its property during such period, without remedy, unless their enforcement should be enjoined. Upon a showing that such reduced rates were confiscatory the Company was entitled to have their enforcement enjoined pending the continuance and completion of the rate-making process.

Id. at 49. *Accord Smith v. Illinois Bell Tel. Co.*, 270 U.S. 587, 591-92 (1926) (company suffering from interim confiscatory rates is not required "to await a decision of the

ratemaking tribunal before applying to a federal court for equitable relief").

To be sure, it may not be possible to determine finally what rates are required prior to completion of a full rate proceeding. To deal with this problem, there is a well-established procedure by which a temporary, interim rate increase may be granted on the basis of a preliminary showing, with the proceeds of that increase to be held in escrow pending conclusion of the rate proceeding, subject to refund (with interest) to whatever extent the interim increase is ultimately found not to have been justified. See *In Re Industrial Sand Rates*, 66 N.J. 12, 25-6, 327 A.2d 427, 434-35 (1974); *New Jersey State AFL-CIO v. Bryant*, 55 N.J. 171, 176-77, 260 A.2d 225, 227-28 (1969). In this way, the regulated company is protected from irreparable loss of revenue to which it is entitled while ratepayers are protected against any ultimate liability for amounts in excess of those which they are in fact obliged to pay.

To be sure, a regulated company is not *routinely* entitled to rate relief prior to completion of a rate proceeding.

"It is true . . . that a utility is entitled to rates that are just and reasonable; but this is not to say that rates must fluctuate automatically with every change in economic conditions or that a reasonable time may not be allowed for determining the reasonableness of a proposed increase in rates before it is allowed to go into effect. Any loss sustained by a maintenance of the status quo while such determination is being made is properly considered, not as a violation of constitutional right, but as a necessary incident of rate regulation so long as the period of

suspension does not 'overpass the bounds of reason.' "

In Re N.J. Power and Light Co., 15 N.J. 82, 90, 104 A.2d 1, 5 (1954), quoting *Hope Natural Gas Co. v. Federal Power Commission*, 196 F.2d 803 (4th Cir. 1952).

But this is not a case in which the rates were previously set to provide a fair and reasonable return as to the very business which the regulated company would be conducting pending the establishment of new rates. In such a case, it may sometimes be proper to presume that those rates remain fair and reasonable until a full hearing has shown otherwise. Here, however, the Commissioner seeks to change the status quo by compelling Allstate to undertake a substantial volume of new business, with characteristics very different than the business for which Allstate's rates were set. Moreover, no fair and reasonable rates were ever previously established for the business Allstate would be forced to take: the JUA rates were always based on cash-flow underwriting (which Allstate is legally forbidden to conduct and which would inevitably confiscate Allstate's property to satisfy obligations for which no reserves would be provided) and, more recently, on a billion-dollar annual subsidy which will not be available to Allstate. Thus, there is no room for any presumption that existing rates are fair and adequate.

Nor is the need for emergency relief the result of any lack of diligence by Allstate. In light of FAIRA's apparent prohibition on recovery of the taxes and assessments it imposed, Allstate acted diligently by applying for rate relief relating to those taxes and assessments in August, promptly after the Commissioner announced the position

that they might be recoverable in some circumstances. (ALa 44A-45A, ¶7) The Commissioner has also indicated, in the litigation relating to that filing, that no action could have been taken on such a filing, even had it been made earlier, because he had not yet developed the standards applicable to such filings.

Allstate also acted diligently in making its October filing promptly after it became possible to estimate (inadequately, as subsequent events have shown) the rate levels to be required in light of FAIRA and related developments. (ALa 44A-45A, ¶7) The October filing was made in time for the Commissioner to act, at least on an interim basis, prior to issuance of depopulation assignments.

In these circumstances, and in the face of a *prima facie* showing that the Depopulation Order will have a confiscatory impact, the Commissioner may not summarily require compliance by simply pointing to a pending rate proceeding which might someday result in prospective elimination of any rate inadequacy.

E. If the Commissioner Chooses To Deny All Rate Relief While Insisting on Compliance With the Depopulation Order, He Must Do So On the Basis of a Judicially Reviewable Determination That No Confiscation Will Result.

This Court may not make rates. *In Re Industrial Sand Rates*, 66 N.J. 12, 19, 327 A.2d 427, 431 (1974). "However, in matters of substantial constitutional dimension the Executive and the Legislature are not the determining or final arbiters." *Valent v. New Jersey State Board of Education*, 114 N.J. Super. 63, 69, 274 A.2d 832, 836 (Ch. Div.

1971). See also *Campbell v. Office of Personnel Management*, 694 F.2d 305, 307 (3rd Cir. 1982) (legislature "cannot preclude judicial review of allegedly unconstitutional legislative action"). Thus, the Commissioner may not be permitted to act as the sole arbiter of an insurer's right not to have its property taken by the maintenance of confiscatory rates while compelling it to take on new business not provided for in those rates.

Because Allstate will have no ability to recover any inadequacy from its policyholders, current or future, the Commissioner will be the sole arbiter if he may, without affording rate relief, compel Allstate to comply with the Depopulation Order in the face of the *prima facie* showing of confiscation made here. That cannot be permitted. See, e.g., *Alaska Public Utilities Comm. v. Greater Anchorage Area Borough*, 534 P.2d 549, 556-60 (Alaska 1975) (denial of interim relief reviewable where rate proceeding likely to be prolonged).

Similarly, if this Court were simply to accept the Commissioner's assurance (which Allstate expects will be forthcoming) that he finds Allstate's rates adequate, the Commissioner would be left as sole arbiter of Allstate's constitutional claims. On the other hand, this court cannot, on the present record, resolve the dispute between Allstate and the Commissioner on that point. But this Court can and should order that the Commissioner not demand Allstate's compliance with the Depopulation Order, absent the rate relief necessary to obviate the confiscatory impact shown *prima facie* by Allstate, until the Commissioner first makes a finding, supported by an administrative record, that no confiscation will, in fact, occur. If such a determination were made and if Allstate

disputed it, this Court could then review the Commissioner's action, so that the Commissioner would not be left to pass an unreviewable judgment on Allstate's claims.

APPENDIX 11

IN THE MATTER OF THE)	SUPERIOR COURT OF
ASSIGNMENT OF)	NEW JERSEY
EXPOSURES TO)	APPELLATE DIVISION
ALLSTATE)	DOCKET NO.
INSURANCE COMPANY)	A-2631-90T5F
and)	
IN THE MATTER OF THE)	SUPERIOR COURT OF
ASSIGNMENT OF)	NEW JERSEY
EXPOSURES TO THE)	APPELLATE DIVISION
AETNA CASUALTY)	DOCKET NO.
AND SURETY COMPANY)	A-2628-90T5F
and)	
IN THE MATTER OF THE)	SUPERIOR COURT OF
ASSIGNMENT OF)	NEW JERSEY
EXPOSURES)	APPELLATE DIVISION
TO COLONIAL PENN)	DOCKET NO. A-2783-90
INSURANCE COMPANY,)	

REPLY BRIEF OF APPELLANT
ALLSTATE INSURANCE COMPANY

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- II. THE COMMISSIONER MAY NOT SIMPLY IGNORE A PRIMA FACIE SHOWING OF CONFISCATION WHEN ATTEMPTING TO COMPEL AN INSURER TO TAKE ON A SUBSTANTIAL VOLUME OF NEW BUSINESS (A) FOR WHICH NO ADEQUATE RATES HAVE EVER BEEN FIXED AND (B) WHICH THE INSURER'S RATES WERE NEVER DESIGNED TO SUPPORT.

The Commissioner makes four responses to Allstate's attack on the validity of compelling it to accept depopulation assignments at inadequate rates. First, he mischaracterizes Allstate's attack as a facial challenge and ignores Allstate's demonstration of a confiscatory effect. (Cb 31) Second, he points to the possibility (already addressed at ALb 54-58) of obtaining some rate relief from flex-rate increases and the filing of a rating plan for non-standard risks. (Cb 32-33) Third, he argues that, as a matter of administrative procedure, this Court may take no action regarding Allstate's claims of confiscation until pending rate proceedings are completed. (Cb 33-34) Finally, he asserts that, as a matter of substantive law, an insurer has no right to adequate rates until completion of a rate proceeding. (Cb 35-38)

- A. Allstate Has Made A Prima Facie Showing That The Depopulation Order Will Have A Confiscatory Effect.

The Commissioner asserts that:

Aetna and Allstate request this Court to find Section 20 of the FAIR Act facially unconstitutional

because under no conceivable set of circumstances could an insurer realize a just and reasonable return.

(Cb 31) This misstates Allstate's argument. Allstate readily admits that the accelerated depopulation mandated by Section 20 of FAIRA *could* be implemented in a way that would allow insurers generally (and Allstate in particular) to realize a just and reasonable return. Thus, Allstate recognizes that Section 20 is not, in and of itself, facially unconstitutional. Rather, Allstate specifically challenges the *manner* in which the Commissioner has implemented that section because, as applied to Allstate, that implementation precludes a just and reasonable return.

Nor does Allstate rely solely on "speculative assumptions on potential losses." (Cb 31) In particular, Allstate does not rely (Cb 31) simply on the fact that its standard rates are too low, for it would utilize MTF rates so long as those rates remain higher than Allstate's own. Rather, Allstate placed before the Commissioner extensive evidence of the inadequacy of its rates to sustain the losses which would result from the new business he now seeks to assign to Allstate. There can be little doubt that the assigned business *will* produce massive losses.

First, the MTF rates Allstate is permitted to charge for this new business are rates which were deliberately set to cover only *immediate* cash flow needs rather than supporting maintenance of the reserves necessary to pay *all* claims resulting from those policies. (ALa 237a; see ALb 17-19) Use of those rates generated a \$3 billion

deficit for the JUA before its existence was terminated. That deficit was created despite the JUA's receipt, over and above the premiums calculated pursuant to its rates, of an enormous subsidy,⁷ which will now cease to exist.

Second, two independent actuarial studies commissioned by the MTF found that its rates needed to be increased by over 60% simply to cover out-of-pocket costs of providing the insurance, with no reward for the exposure of capital to the risks of that insurance. (ALa 187a-227a) Even the Insurance Department recognized that the MTF rates are inadequate to operate on the statutorily-required "no-profit, no-loss" basis and that at least a 28% increase in those rates is necessary.⁸ (ALa

⁷ In Allstate's opening brief, this subsidy was estimated at "almost \$1 billion annually." (ALb 28 n.10) For 1989, the precise amount was \$810,326,504. *Annual Statement of the New Jersey Automobile Full Insurance Underwriting Association to the Department of Insurance for the State of New Jersey for the Year Ended December 31, 1989* 18. Given increases in the number of insured vehicles, the figure for 1990 would be roughly \$900 million. For present purposes, the exact magnitude of the figure does not matter. It is enough that it is enormous.

⁸ The refusal to recommend a larger increase was *not* based on any question as to the validity of the showing that a 60% increase was required. Rather, it was explicitly based on a desire not to increase the rates of "good drivers" in the MTF by more than the 9.4% "flex-rate" increase necessary to allow for inflationary cost increases, *regardless of whether such an increase was adequate to cover the costs of their insurance.* (ALa 146a)

145a-46a) Allstate's own actuaries project an average annual loss of \$634 per policy at MTF rates. (ALa 43a)

Moreover, the risks to be assigned are not merely an average group of JUA/MTF risks, with an average level of rate inadequacy. They are risks systematically selected from the rate territories least attractive to private insurers. As Deputy Commissioner Grubb found, statutory rate-capping requires that rates in the highest-risk territories⁹ be set at levels significantly below levels reflecting actual territorial loss costs. (ALa 84a) Thus, even were JUA/MTF rates adequate, on average, for all the risks they insure, they would necessarily be inadequate for the subset of those risks which are located in the capped territories. When rates are not adequate, on the average, as the record shows MTF rates are not, the rates for risks in the capped territories will necessarily be more inadequate than average.

⁹ Those territories are urban territories. Allstate does not contend, as the Commissioner suggests (Cb 34), that "urban drivers are . . . *per se* bad drivers." Allstate simply contends that drivers in those areas have substantially higher losses than those in other areas. This may just reflect the greater accident frequency to be expected with greater traffic density, or there may be other reasons as well. But whatever the cause of this higher risk level, it is a fact. (ALa 84a) That fact must be taken into account in assessing the adequacy of the rates charged to a population disproportionately composed of drivers from those territories.

Similarly, Allstate has presented evidence of the inadequacy of its own rates to cover the costs of insuring its present customers, let alone the losses to be produced by the assignments made by the Depopulation Order. (ALa 43a-45a; Asa Tabs 12, 13) Specifically, Allstate projects a 1991 operating loss of \$111 million on New Jersey auto insurance business (including over \$20 million attributable to the assigned business) and a substantial operating loss on its entire New Jersey insurance business.¹⁰

Another way of looking at Allstate's prima facie showing is in terms of the presumptions flowing from operation of the regulatory structure. Once rates have been fixed which are just and reasonable, they are presumed to remain just and reasonable until the contrary is

¹⁰ The Commissioner has included in his appendix testimony purporting to show that Allstate made money in the period 1985-89. (Ca 199A-200A) Lest this Court uncritically accepts that showing, Allstate mentions a few of the most important errors in this information. First, it included in the profit stated the return Allstate received from investment of the capital with which it backed its New Jersey policies. That income would be available even if Allstate did not engage in the insurance business and need not be credited to shareholders in fixing a just and reasonable return for that business. See, e.g., *In re Application of Insurance Rating Board*, 63 N.J. 413, 414-19, 307 A.2d 604, 605-07 (1973). Second, the data fails to reflect certain sizeable dividends which Allstate paid to policyholders to eliminate excess profits otherwise refundable under *N.J.S.A. 17:29A-5.6-5.16*. Third, the time period is distorted because elimination of the financially draining assigned risk business through formation of the JUA temporarily produced unusual profits in 1985 and 1986, which were not repeated in 1987-1990, and will not be repeated in 1991 or subsequent years.

shown. See, e.g., *Swift & Co. v. United States*, 343 U.S. 373, 382-83 (1952). Where, as is the case with the JUA/MTF rates, rates were deliberately set at a level which was not just and reasonable, then it should likewise be presumed that they have not spontaneously become just and reasonable.

Nor can this presumed inadequacy on the assigned business be made up by any excess profit on Allstate's other business. Allstate's present automobile insurance rates were approved by the Commissioner long before FAIRA.¹¹ Even if, despite FAIRA's imposition of new taxes and assessments, Allstate's rates could be presumed to remain adequate for the voluntary business with respect to which those rates were set, they surely must also be presumed not to be excessive for that business. Accordingly, the voluntary business would provide no excess profits which could subsidize losses from the depopulation assignments. Thus, the Commissioner's own system of rate regulation supports a presumption that the Depopulation Order *will* have a confiscatory effect on Allstate.

Most of this evidence was presented to the Commissioner, in rate applications, well before he issued the

¹¹ Allstate's last general rate increase took effect in March, 1989. Since that time, Allstate has also taken two flex-rate increases, which are designed simply to protect Allstate against inflationary cost increases. *N.J.S.A.* 17:29A-44a. The Commissioner has the power to limit flex-rate increases if he believes that they will produce excessive rate levels. *N.J.S.A.* 17:29A-44d.

Depopulation Order. Its relevance was called to his attention on a motion for an administrative stay of that Order.¹² The issue before this Court is whether he was free to simply ignore this evidence and demand compliance with the Depopulation Order despite a *prima facie* showing that the Order would have a confiscatory effect.

B. The Commissioner May Not Simultaneously Demand Both Immunity From Judicial Review And Immediate Compliance With a Final Order Which Has Been Shown Prima Facie To Be Confiscatory.

The Commissioner argues that this Court cannot determine the adequacy of Allstate's rates on the record now before it "without the benefit of a hearing and decision below." (Cb 31) Allstate recognizes that this is true and does not ask this Court to make such a determination.

Many of the cases cited by the Commissioner (Cb 32, 37) are concerned with the need for a full factual record and/or with protection of the integrity of the administrative process and its ability to sift through the underlying

¹² The Commissioner could have acted at any time, at least on an interim basis, to permit the requested increases in Allstate's rates. Similarly, he might have acted at any time to allow an increase in the MTF rates. Finally, the precise terms and content of the Depopulation Order were not clear until he issued it. Thus, not until the Depopulation Order was issued *without* any action on the proposed rate increases was there a clear basis for presenting a more detailed claim based on the confiscatory impact of the Depopulation Order itself. Allstate presented that claim promptly after it arose.

facts before any judicial determination is made regarding those facts. Allstate recognizes these concerns as well, and does not seek any substantive consideration of whether its rates are actually adequate, either generally or for the depopulation business the Commissioner seeks to assign.

But this is not a case where judicial intervention is "premature" – Allstate is subject to a final administrative order. Despite Allstate's *prima facie* showing that the Depopulation Order will have a confiscatory effect, the Commissioner demands immediate compliance, thereby threatening irreparable harm to Allstate. Judicial review at this juncture is both timely and essential to protection of substantive rights.

Finally, this is not a case where *Allstate* seeks alteration of the status quo by demanding an increase in the rates charged on its existing business. Compare *Public Util. Comm'n v. Pedernales Elec. Coop.*, 678 S.W.2d 214 (Tex. App. 1984). It is *the Commissioner* who seeks to change the status quo by requiring Allstate to take on a vast quantity of new business whose costs and risks differ from its existing business.

Where judicial review is essential but administrative proceedings are a necessary predicate to an ultimate decision, it is proper to require that the administrative process be conducted in a way which will accommodate both needs. See, e.g., *State Farm Mutual Auto Ins. Co. v. State*, 118 N.J. 336, 348-50, 571 A.2d 957, 963-64 (1990); *Abbott v. Burke*, 100 N.J. 269, 297-98, 495 A.2d 376, 391-92 (1985). That is what Allstate proposes here.

Under the procedure Allstate suggests, further administrative review of an order said to have a confiscatory effect would be triggered upon presentation to the Commissioner of a *prima facie* showing of that effect. The Commissioner could then take any of a number of actions. First, he could allow rate relief sufficient to obviate the effect shown. This could be final relief if that were appropriate, but could also be temporary, interim relief pending further review (and subject to refund if that review showed it not actually justified). Second, he could withdraw, modify, or defer the order said to produce the confiscation, again obviating the forbidden effect. Third, he could examine the underlying facts and make a determination that no relief is necessary because no confiscation would result.

Whichever course the Commissioner took, his action could be judicially reviewed on an appropriate record. What the Commissioner would not be permitted to do is what he did here: ignore the showing of confiscation, demand immediate compliance, and claim that judicial consideration of the confiscation claim is barred because that claim was not resolved administratively.

The procedural scheme Allstate suggests both protects against abridgment of the substantive constitutional right not to have property taken without just compensation and respects the primacy of the Commissioner in his legislatively delegated sphere. No issue would be adjudicated until the agency has passed on it. Nor does this procedure demand impossible speed in resolving what may be difficult questions presented by the confiscation claim. If appropriate, the allegedly confiscatory order may be stayed pending such resolution. If some other

public interest demands more immediate compliance with that order, then interim rate relief may be granted, protecting against irreparable harm either to the insurer (who will be permitted to collect the necessary revenue and to retain it if the increase is found to have been justified) or to its customers (who will be assured of refunds, with interest, if the increase is found not justified).¹³

C. The Constitution Does Not Permit Confiscation Of Property To Be Accomplished By Imposition Of New Public Duties Without Adjustment Of Pre-Existing Rates, Even During The Pendency Of A Rate Proceeding.

The Commissioner boldly asserts that it would not matter even were it established that confiscation would

¹³ Without such a procedural scheme, one of two alternatives must be accepted. First, the aggrieved insurer could be permitted to seek direct judicial intervention, in the nature of an injunction, in which proceedings its claims of confiscation would be assessed by a court in the first instance. This is surely not what the Commissioner urges here, and it would sacrifice the benefits of initial administrative consideration. See *United States v. RCA Alaska Communications, Inc.*, 597 P.2d 489, 494-95 (Alaska 1979) (court may adjudicate utility's right to interim relief, but must do so solely by reviewing administrative record and findings). What he does urge is the only remaining alternative, that the insurer claiming confiscation be left solely to the grace of the Commissioner to protect its rights. That alternative, however, would unlawfully sacrifice substantive constitutional rights to mere procedural convenience. Cf. *Smith v. Director, Division of Taxation, supra*, 108 N.J. at 33, 527 A.2d at 850 (procedural convenience does not justify abrogation of statutory rights).

result from imposition of depopulation assignments without alteration of current rates, because "[d]ue process rights may be diminished, by the imposition of confiscatory rates, pending a final administrative hearing on a request for increased rates." (Cb 37) But even the line of cases he cites does not support that proposition, and especially not in this context.

At most, those cases support the proposition that where a company has voluntarily assumed a duty to provide public service as a utility and rates have been established for the performance of that duty, the regulator may be entitled to briefly maintain the status quo pending review of a request for an increase in the rates for the existing public service.¹⁴ But Allstate has not voluntarily undertaken a duty to provide public service; that duty has been imposed upon it against its will by

¹⁴ Most of these cases also depend heavily on the need to refrain from premature intervention in the administrative process. As just shown, that problem is not presented here. Moreover, *Public Util. Comm'n v. Pedernales Elec. Coop.*, 678 S.W.2d 214, 222-23 (Tex. App. 1984), relied on the statutory right of the utility there to implement an interim increase if the effective date of its increase was delayed 90 days, as has happened here. It does not support legality of the instant prolonged and indefinite delay.

Additionally, the leading case in this line (and several subsequent cases) involved an attempt to obtain retroactive application of a rate subsequently approved to a period before its approval. *Hope Natural Gas Co. v. FPC*, 196 F.2d 803, 804 (4th Cir. 1952). Even had the prior rates in that case been confiscatory, that attempt would have violated the requirement that all ratemaking be purely prospective. See *In re Industrial Sand Rates*, 66 N.J. 12, 23, 327 A.2d 427, 433 (1974).

enactment of the JUA depopulation statute and FAIRA. Allstate's rates were never set to cover performance of its newly imposed public duties, so they cannot be presumed adequate for those duties. And the regulator is not maintaining the status quo but altering it by demanding performance of onerous new duties without any corresponding adjustment of the rates allowed as compensation for the service to be provided.

Even in the special context presented by the Commissioner's line of cases, there can be a right to timely rate relief before completion of lengthy rate proceedings. As the Michigan Supreme Court has explained:

A public utility has a substantive right, set forth in the statutes and rooted in the constitution, to rate relief where the revenue produced by an existing rate structure is less than the amount required by the statutes or the constitution. A public utility has, as a corollary to that substantive right, a right to immediate relief where compelling circumstances indicate that such relief is necessary.

* * *

The substantive right to rate relief includes the right to a determination, following a hearing if necessary, whether immediate or permanent relief shall be granted.¹⁵

¹⁵ *Consumers Power Co. v. Michigan Public Service Comm'n*, 415 Mich. 134, 145, 327 N.W.2d 875, 878-79 (1982) (footnotes omitted) (affirming judicial order permitting interim rate increase pending completion of rate proceedings, denied by regulator); *Alaska Public Utility Comm'n v. Greater Anchorage*

(Continued on following page)

The New Jersey Supreme Court has also recognized that interim relief, prior to completion of a rate proceeding, is sometimes necessary to permit a regulated business "to escape the unfair and sometimes confiscatory impact of 'regulatory lag' i.e., the considerable time necessary for final resolution . . . of a rate increase." *In Re Industrial Sand Rates*, 66 N.J. 12, 25, 327 A.2d 427, 434 (1974) (emphasis added).

That such form of relief is necessary on the facts here may be seen from *Calfarm Insurance Co. v. Deukmejian*, 48 Cal. 3d 805, 258 Cal. Rptr. 161, 771 P.2d 1247 (1989).¹⁶ There, the services required from insurers were not changed, but their rates were to be rolled back 20% by statute. The effect obviously would be similar to requiring increased services and leaving the rates unchanged. To sustain the constitutionality of the statute, it was found *necessary* to provide insurers with the opportunity to obtain interim relief if they could show that either the statutory rollback or, subsequently, the delay

(Continued from previous page)

Area Borough, 534 P.2d 549, 558 (Alaska 1975) (same); *City of Tyler v. Television Cable Service, Inc.*, 481 S.W.2d 166, 172 (Tex. Civ. App. 1972) (utility entitled to interim judicial relief to prevent irreparable harm from occurring while it exhausted its remedies before regulatory body).

¹⁶ *Calfarm* relied upon and further developed the principles laid down in *Hutton Park Gardens v. Town Council*, 68 N.J. 543, 350 A.2d 1 (1975), and *Birkenfeld v. City of Berkeley*, 17 Cal. 3d 129, 130 Cal. Rptr. 465, 550 P.2d 1001 (1976). The *Birkenfeld* analysis was itself followed in *Helmsley v. Borough of Fort Lee*, 78 N.J. 200, 226, 394 A.2d 65, 76-78 (1978), *app. dism'd*, 440 U.S. 978 (1979). Thus the analysis utilized in *Calfarm* has been approved by the New Jersey Supreme Court.

incident to a rate proceeding, would have a confiscatory effect. *Id.* at 816-26, 258 Cal. Rptr. at 166-73, 771 P.2d at 1252-59. With respect to the statutory rollback, insurers were permitted to continue using their existing rates (without any rollback, subject to future refund if later found excessive) until the regulator determined what rates were proper.¹⁷ *Id.* at 825, 258 Cal. Rptr. at 172-73, 771 P.2d at 1258-59.

It has long been recognized that "[p]roperty may be as effectively taken by long-continued and unreasonable delay in putting an end to confiscatory rates as by an express affirmance of them." *Smith v. Illinois Bell Telephone Co.*, 270 U.S. 587, 591 (1926). Regulatory delay is surely unreasonable where the regulator himself proposes to heap costly new duties on the regulated industry while refusing to permit concomitant rate increases necessary to permit just and reasonable compensation for performance of those new duties. If a confiscatory effect is shown

¹⁷ A lower California court later held that an insurer seeking a rate *increase* may be forced to wait a reasonable time for completion of a rate proceeding without any right to interim relief. *Allstate Ins. Co. v. Gillespie*, 275 Cal. Rptr. 525, 538-42 (Cal. App. 2d Dist. 1990). Even were *Gillespie* correctly decided, it would be inapposite here. It relied primarily on the need to avoid premature interference in the administrative process, a problem not presented here. It also involved maintenance of the status quo rather than its alteration by imposition of new duties or reduction in rates for existing duties. However, the California Supreme Court has indicated serious doubts, at the very least, about *Gillespie's* correctness by ordering that it not be published in the official reports, thereby depriving it of any precedential effect. *Allstate Ins. Co. v. Gillespie*, No. S014332 (Cal. Feb. 21, 1991); see Cal. R. 977(a)(forbidding citation of unpublished opinions).

prima facie, such duties should not be imposed without *either* providing the rate adjustment necessary to obviate the confiscation shown *or* determining that contrary evidence rebuts the prima facie showing.

APPENDIX 12

ORDER NO.: A91-212

STATE OF NEW JERSEY
DEPARTMENT OF INSURANCE

IN THE MATTER OF THE)
JANUARY 17, 1991 RATE FILING) DECISION
BY THE MARKET TRANSITION)
FACILITY OF NEW JERSEY)

The Market Transition Facility of New Jersey (MTF) submitted a rate filing to the Commissioner of the New Jersey Department of Insurance (Commissioner) on January 17, 1991. The filing proposed a number of changes to the existing MTF rating plan. According to this filing, approval of all the requested changes would raise the average MTF rate by 28%.

The following specific rating plan revisions were proposed on January 17, 1991,

- a. the elimination of the Driver Improvement Program (DIP) and, in its place, the substitution of the Driving Record Debit Plan (DRDP);
- b. the elimination of the second rating tier (Tier II) from the MTF rating plan;
- c. a flex rate increase;
- d. the introduction of various penalty fees to be charged in addition to the otherwise applicable premium; and,
- e. a premium payment plan with six installments including upfront collection of the installment fees.

An amended version of the premium payment plan was submitted to the Commissioner on April 18, 1991. The revised plan maintained the number of payments (six) and the length of the plan (nine months), but changed the amount of the different installments.

Underlying the January 17, 1991 rate filing was an analysis of the rate increase necessary to bring the MTF to a breakeven financial condition. Two independent actuarial evaluations of the MTF's financial condition were obtained to provide this information. One, by William M. Mercer, Inc., (Mercer) was commissioned by the insurance industry under the auspices of the MTF Advisory Board's Actuarial Committee. The other, by Milliman & Robertson, Inc., (Milliman) was requested by the MTF itself.

The conclusion of the Milliman report, as stated in a November 2, 1990 letter to Mr. Lewis Roberts, an Assistant Commissioner in the Department of Insurance, was:

... , we estimate that the rate level implemented for the MTF on October 1, 1990 was deficient by 62.2%. The indications by line show that virtually all of the inadequacy comes from the liability coverages which are deficient by 97.7% whereas the Physical Damage coverages are nearly adequate with a deficiency of only 6.0%.

The findings of the Mercer study were similar with the overall rate shortfall estimated to be 58.0%, based on a Liability coverage inadequacy of 88.5% and a Physical Damage deficiency of 7.5%.

The Department of Insurance began its review of the January 17, 1991 MTF rate filing shortly after its submission to the Commissioner. This process was completed recently. The determinations made hereinafter are based upon the following documents – (1) MTF Filing for Rate Revision, dated January 17, 1991; (2) Milliman & Robertson, Inc. report entitled “New Jersey Market Transition Facility: Analysis of Rate Level Needs as of October 1, 1990”, dated November 2, 1990; (3) William M. Mercer, Inc. report entitled “New Jersey Private Passenger Automobile Market Transition Facility”, dated November 14, 1990 – and the Department of Insurance staff evaluation of these documents.

I. MTF Physical Damage Coverage Rate Indication

According to both actuarial studies of the MTF, the current MTF physical damage coverage rates are close to adequate at the present time, at least on an overall basis. The specific indications estimated by Mercer and Milliman for these coverages were,

<u>Coverage</u>	<u>Mercer</u>	<u>Milliman</u>
Collision	- 1.0%	+4.4%
Comprehensive	+22.5%	+8.7%
Overall	+ 7.5%	+6.0%

However, in order to evaluate these recommendations properly, it is critical to review the accuracy of the assumptions underlying the calculations. This analysis can be found below.

a. Analysis of Mercer Physical Damage Indications

The Mercer overall physical damage coverage indication of a 7.5% rate increase is predicated on depopulation of the MTF. Specifically, Mercer has assumed an MTF market share of 35% in the fourth quarter of 1990, 29% in the first and second quarter of 1991. In actuality, the voluntary market has been depopulating the MTF at a slower rate than was assumed by Mercer.

On October 1, 1990, the MTF market share was 37.4%. The MTF's market share on January 1, 1991 was 36.4%. Recently, the Department received private passenger automobile insurance market share data for April 1, 1991. On that date, the MTF share of the market was 34.4%.

The Mercer report also contains an evaluation of how slower depopulation will affect the MTF's rate inadequacy. According to Mercer's own calculations, slower depopulation reduces the all coverage rate increase to 51.5%, a noticeable decrease from the original shortfall estimate of 58.0%. Because depopulation has occurred more slowly than Mercer assumed, a more accurate estimate of the physical damage coverage rate indications are the values from the Lesser Depopulation Effect analysis in the Mercer report. These amounts are,

Collision, -2.5%

Comprehensive, +10.5%

The overall physical damage rate indication, assuming slower depopulation, is +2.5%.

b. Analysis of the Milliman Physical Damage Indications

The Milliman physical damage rate indication calculations also are based on overly optimistic assumptions about MTF market share. Milliman assumed a 32% market share for the first six months of MTF operation, a period which ended April 1, 1991. As noted above, the MTF insured a larger percentage of the market from October 1, 1990 through March 31, 1991.

The impact of slower than anticipated depopulation on the Milliman physical damage rate increase is somewhat unclear. As stated in the report, Milliman's findings do not reflect any worsening of MTF loss experience as a result of depopulation. However, the Milliman report does indicate that depopulation is expected to result in the MTF's losing its better-than-average insureds. Arguably, therefore, the absence of depopulation should not worsen the results and the Milliman estimates should be regarded as upper bounds on the required rate increase.

In calculating the indicated physical damage rate changes, Milliman has assumed a collision loss trend rate of 9.1% and a comprehensive loss trend amount of 10.5%. Mercer's trend values for these two coverages are lower, 7.0% for collision and 9.0% for comprehensive. The Milliman trend values appear overly cautious, given the choices that Mercer has made. Using the Milliman rate calculation methodology with the more reasonable trend rates recommended by Mercer, the Department staff has determined that the indicated physical damage rate indications would be,

Collision, -3.5%

Comprehensive, +2.8%

When these individual coverage results are combined, the MTF physical damage rate indication is -1.1%.

Another concern is Milliman's use of the New Jersey Automobile Full Insurance Underwriting Association's (JUA) combined results for accident years 1985-1989 in calculating the MTF rate change indications. The indicated collision coverage rate inadequacy, for example, is substantially lower for accident years 1988 and 1989 combined (+0.5%) than for the 1985, 1986, and 1987 period (+7.3%). A similar result can be observed for the comprehensive coverage where the last two year rate inadequacy (+5.0%) is well below the deficiency for accident years 1985 through 1987 (+11.2%).

Given the apparent dissimilarity of the first three and last two years of the experience period, the five individual accident years probably should not be combined for the purpose of estimating the physical damage coverage rate needs of the MTF. And, by choosing to analyze the available data on an all accident year combined basis, Milliman may have overstated the MTF rate inadequacy for these two coverages.

c. Selected Physical Damage Rate Indications

Neither actuarial study of the MTF has indicated a need for a substantial physical damage rate increase on an overall or combined coverage basis under the conditions assumed in each of these reports.

It is evident, however, that depopulation of the MTF is occurring more slowly than anticipated by either Mercer

or Milliman. Slower than expected depopulation, according to Mercer, reduces the MTF's need for a physical damage rate increase. The Milliman report does not address this issue directly, but a reduced depopulation rate should not worsen the physical damage rate indications, because Milliman does expect that the best insureds in the residual market will be depopulated first.

The Milliman results also could overstate the MTF's collision and comprehensive rate needs because of excessively conservative assumptions about future loss trends. Another consideration in evaluating the Milliman findings is that the results are based on the JUA loss experience for the entire period 1985-1989, rather than only the latest two years when the indications were more favorable.

One actuarial study of the MTF's physical damage coverages indicates a small rate inadequacy while the other shows that these rates may be slightly too high. These same studies agree that collision rates may be somewhat more than adequate while comprehensive premium levels could be a little too low. In general, the indicated changes are not substantial for either coverage.

Given the general similarity of the two actuarial analyses, it is appropriate to use the average of the Mercer and Milliman results as the selected rate indications. These values are Collision, -3.0%, and Comprehensive, +6.7%.

II. MTF Liability Coverage Rate Indication

The Mercer and Milliman MTF actuarial studies contain the following rate level indications for the three different liability coverages:

<u>Coverage</u>	<u>Mercer</u>	<u>Milliman</u>
Bodily Injury	+ 77.5%	+ 93.9%
PIP	+177.0%	+173.0%
Property Damage	+ 35.5%	+ 31.2%
Overall	+ 88.5%	+ 97.7%

As before, the accuracy of the assumptions generating these numbers must be assessed in order to determine whether these indications should be accepted or not. This discussion can be found below.

a. Analysis of Mercer Liability Indications

As was the case for the physical damage coverages, the Mercer liability rate indications assume substantive depopulation of the MTF. Actual events have proven this assumption false and, by Mercer's own calculations, slower depopulation decreases the MTF's rate needs.

The Mercer liability coverage indications when depopulation of the MTF occurs more slowly than was assumed in the base case analysis are,

Bodily Injury, +69.5%
 PIP, +166.0%
 Property Damage, +34.5%
 Overall, +81.5%

b. Analysis of Milliman Liability Indications

As discussed in Section I, there is no simple way to restate the Milliman results to reflect the MTF's greater than anticipated market share. However, the failure of the voluntary market to depopulate the MTF should reduce the otherwise indicated estimate of the liability rate shortfall by leaving more good drivers in the residual market than the Milliman analysis anticipated.

In developing the liability rate change indications, Milliman again appears to have been extra-conservative in the selection of the loss trend rates. A comparison of the selected trend factors from the two MTF actuarial studies is provided below.

Coverage	Mercer Trend Rate	Milliman Trend Rate
Bodily Injury	+ 6.5%	+10 8%
PIP	+ 9.0%	+15.1%
Property Damage	+ 7.0%	+ 9.0%

Substitution of the lower Mercer trend rate assumptions into the Milliman MTF financial model necessarily lowers the rate indications for each coverage. After making this change, the rate indications for the individual liability coverages are,

Bodily Injury, +66.9%
 PIP, +121.9%
 Property Damage, +22.6%
 Overall, +69.3%

c. Selected Liability Rate Indications

After adjusting the liability coverage results in both MTF actuarial studies to recognize the true pace of depopulation and the expected loss trend rates, the overall liability rate indications are – Mercer, +81.5%, and Milliman, +69.3%. Although these two rate deficiency forecasts do differ, almost all of the variation is attributable to a disagreement about the estimated size of the PIP coverage rate shortfall.

Again, there is no specific reason to consider the findings of one study more “accurate” than those of the other. Accordingly, the average of the Mercer and Milliman liability rate shortfall values has been chosen as the selected indication for each coverage. The resulting figures are Bodily Injury, +68.2%, PIP, +144.0%, and Property Damage, +28.6%.

III. Other Rating Considerations

The selected rate indications in sections I and II above do not represent the only concerns relevant to the Commissioner in making a determination on the MTF Filing for Rate Revision dated January 17, 1991. These other considerations are discussed below and the rating impact of each issue is assessed as part of the Commissioner’s evaluation of the MTF filing.

a. Elimination of the Tier II Rating

The January 17, 1991 filing is premised on several changes to the current MTF rating plan. One requested

revision is the elimination of the second MTF rating tier, more commonly known as "Tier II".

Tier II rates are charged to any MTF policyholder who has had (i) at least one at fault accident, (ii) two or more moving violations, or (iii) more than four motor vehicle points in the 36 month period preceding the policy effective date. All other MTF insureds are charged Tier I rates because of their demonstrably better driving record. The rationale of Tier II rating is to charge more to those insureds who cause or are expected to cause losses.

Section 40 of the Fair Automobile Insurance Reform Act of 1990 (FAIR Act) requires the Commissioner to promulgate a private passenger rating plan wherein the most important factor is the insured's driving safety record. The driving safety record is defined to include motor vehicle points, at fault accidents, and non-point producing moving violations.

The similarities between the Tier II rating rules and the language of FAIR Act Section 40 are striking. Given these similarities, the continued use of the Tier II rating differential is warranted. Accordingly, the MTF request for the elimination of Tier II is disapproved.

b. Elimination of DIP and Substitution of DRDP

Another requested change in the current MTF rating plan is the elimination of the DIP by substituting a similar system known as DRDP. The advantage of DRDP that is cited in the MTF rate filing is its "simplification" of the more complicated DIP. In addition, DRDP surcharges the rates to be paid by MTF insureds on the basis of the FAIR

Act eligibility point system recently promulgated by the Department of Insurance. Since the DIP is not based upon eligibility points, the substitution of the DRDP is appropriate.

However, the DRDP system cannot be approved as originally filed by the MTF. In its January 17, 1991 filing, the MTF proposed a DRDP in which an insured's premium rate would be increased by a specified percentage depending upon the number of eligibility points. The recommended percentage charges ranged from 0% for insureds with 0 eligibility points to 250% for drivers with 14 or more.

The Department has been informed by the Division of Law that the rate surcharge for an at fault accident must be a flat dollar amount, not a percentage charge, to be consistent with N.J.S.A. 17:29A-35. To conform with this requirement, the Department of Insurance staff has developed an amended DRDP for the MTF at the request of the Commissioner. In this revised plan, flat amounts were chosen to approximate what the percentage charge for at fault accidents would have been under the originally filed DRDP. These values are as indicated below.

<u>At Fault Accident</u>	<u>Average Flat Charge</u>
First, Second	\$620
Third, subsequent	\$420

In addition, the approved MTF DRDP will use a different schedule of percentage increase charges for non-accident related eligibility points. It was necessary to change the original eligibility point percentage change values to

reflect the fact that at fault accident charges must be flat dollar amounts. The new schedule of percentage charges for eligibility points that are not produced by at fault accidents can be found in Appendix A of this Order.

c. MTF Flex Rate Increase

The MTF has requested a 9.4% flex rate increase to offset anticipated inflationary effects on claim costs that affect both the voluntary and involuntary private passenger automobile market. This request is disapproved for the reasons indicated below.

Flex rating, as permitted by N.J.S.A. 17:20A-44, is limited to voluntary market insurers. The flex rate statute also specifies how the maximum permissible annual rate increase is to be calculated for each private passenger automobile coverage. In May of each year, the Department uses these rules to calculate the permissible rate increases for a one year period beginning July 1. This information then is transmitted by order to all private passenger automobile insurers.

Because the Department has not established the flex rate increase amounts for the period July 1, 1991 to June 30, 1992, the MTF's requested increase of 9.4% may be excessive. In addition, the proposed effective date, April 1, is prior to July 1. Finally, the MTF is not a voluntary market insurer and it is not entitled to make use of the provisions of N.J.S.A. 17:29A-44. For all of these reasons, the Commissioner cannot grant the MTF's flex rate increase request.

d. Introduction of Penalty Fees

The MTF rate filing requests the ability to impose penalty fees on its insureds for various violations not included in its DRDP. These charges are for activities such as loaning or borrowing a driver's license, allowing an unlicensed driver to operate the vehicle, or using a vehicle without the permission of the owner.

All of the violations generating penalty fees do reflect negatively on the insured's driving safety record. Accordingly, the MTF penalty fee schedule is approved. However, because the MTF filing does not show any rate impact from the adoption of the penalty fee schedule, none is assumed in this determination.

e. Amendment to the MTF Premium Payment Plan

The MTF has sought approval to change its current premium payment plan from a six month, four installment program to one with six installments paid over nine months. As required by N.J.S.A. 17:33B-11(c)(6), the MTF must have an installment payment plan with a period of not less than nine months.

The original proposal for a six payment, nine month plan satisfies this requirement. On April 18, 1991, the MTF filed an amendment to its payment plan proposal reducing the amount of the initial installment and slightly increasing the size of the latter payments. The number of payments, the length of the plan, and the upfront collection of installment fees were not changed. Accordingly,

the revised MTF payment plan still satisfies the requirements of N.J.S.A. 17:33B-11(c)(6) and the April 18, 1991 payment plan is hereby approved.

Neither the original MTF rate revision request nor the April 18, 1991 filing indicate any rate impact from the approval of a six installment, nine month premium payment plan. Consequently, no rate impact is assumed in this determination.

IV. Financial Impact of the Approved MTF Rating Plan Changes

The January 17, 1991 MTF Filing for Rate Revision proposed various changes in the current MTF rating program. According to that filing, the approval of all the requested changes would result in an overall rate increase of 28%. It has been necessary, for the reasons given in Section III above, to reject or to amend some parts of the MTF rate revision request. The approved MTF rating plan will contain the following elements:

- A. a set of Tier I rates;
- b. a set of Tier II rates;
- c. at fault accident surcharges;
- d. rate surcharges depending upon events other than at fault accidents; and,
- e. a six installment, nine month premium payment plan.

The Department of Insurance staff has been asked by the Commissioner to analyze the financial impact of this rating plan because elements b, c, and d differ from the original MTF rate revision proposal. Based upon a review

of approximately 4,000 MTF policies, the Department's actuaries have calculated that the new MTF rating plan will produce an 18.6% increase in MTF revenues.

V. The Need for an Additional MTF Rate Increase

a. Actuarial Evaluation of MTF Rate Adequacy

Two different actuarial firms, William M. Mercer, Inc. and Milliman & Robertson, Inc., had estimated the overall MTF rate deficiency to be about 60%. It already has been determined that both of these studies overestimated the MTF's rate needs by inaccurately forecasting the pace of depopulation. After adjusting the calculations to reflect actual MTF depopulation and other considerations, the Mercer estimate of the required rate increase drops to 51.5% and Milliman's is reduced to 43.3%.

The average of the Mercer and Milliman indications is 47.4%. If the MTF does require a rate increase of this size, the decisions (1) to retain Tier II rating, and (2) to substitute the amended version of DRDP for DIP rating will provide some of the necessary funds. The approved changes to the MTF rating plan are expected to generate 18.6% more premium dollars. Nevertheless, the actuarial evaluations appear to indicate that the MTF needs a further rate increase of 24.3% ($1.474/1.186 = 1.243$) to reach a breakeven financial position.

b. The Accuracy of the MTF Actuarial Evaluations

Critics of this decision probably will use the two MTF actuarial studies to claim that the Department has

underfunded the MTF deliberately. There are several reasons, however, to question whether the actuarial estimates of the MTF rate needs are accurate. Foremost amongst these issues is the actuaries' reliance on JUA data to forecast MTF results.

i. Use of JUA Data: Questions about the credibility of the actuarial findings can be raised, for example, because of the January 1, 1989 introduction of the verbal threshold and the PIP deductibles. The MTF actuarial evaluations include only one year of JUA experience with these coverage changes. Unfortunately, bodily injury and PIP losses take a relatively long time to develop. One year of experience may represent an insufficient basis from which to determine the rate effect of the verbal threshold and the PIP deductibles.

The potential for new programs or coverage changes to improve loss experience is demonstrated by recent JUA physical damage loss experience. As part of the automobile insurance reforms introduced on January 1, 1989, the standard physical damage coverage deductible was raised to \$500. Collision and comprehensive claims settle much more quickly than bodily injury and PIP liability losses, making the JUA physical damage data a somewhat better basis for judging the effect of the 1989 coverage changes. As shown in the Milliman report, the best JUA results for both collision and comprehensive were produced in 1989, after the standard deductible was increased.

The passage of the FAIR Act in early 1990 raises additional questions about the propriety of using JUA data to forecast MTF results. The FAIR Act has changed the

mechanics of the New Jersey private passenger automobile market by providing new coverage options and imposing additional duties on insurers. Two examples of such changes are the health insurance primary PIP option and the mandatory physical damage inspection program. At this time, one can only speculate what savings will be generated by these initiatives.

ii. Operational Differences between the JUA and the MTF: The issue of whether JUA experience is a proper basis for estimating MTF financial needs also can be raised from an operating perspective.

The MTF has four servicing carriers, all of whom are handling relatively large volumes of business and are carry-over JUA servicing carriers. The JUA originally had 15 servicing carriers, three of whom discontinued operations after a short period. Then, the remaining 12 servicing carriers were replaced by five others, four of whom had not handled JUA business previously. The most inefficient of these five did not continue as an MTF servicing carrier.

The JUA began operation in 1984. By early 1985, the JUA share of the New Jersey private passenger automobile market was approximately 40%. The JUA continued to grow slowly until, in mid-1988, about 50% of all New Jersey drivers were insured by the JUA. On September 30, 1990 when the JUA stopped writing business, its market share was still 37.4%.

The MTF's market share, in contrast, probably will peak at less than 35% on September 30, 1991 and could be as low as 10% on September 30, 1992 when the MTF closes its doors. Clearly, the JUA had a much more stable book

of business than the MTF will. Given this difference, it is reasonable to question whether the experience of the MTF will be comparable to that of the JUA.

iii. Other Rate Related Issues: It also is important to recognize that the MTF will continue to write business for another 16 months. The length of this period does provide the MTF with ample time to make another rate application to the Commissioner if its financial results are as poor as the actuaries are predicting.

c. Selected MTF Rate Change Amount

There is substantial uncertainty about depopulation and, correspondingly, the performance of the MTF. The actuarial analyses are based solely on the experience of the JUA, not the MTF. The MTF financial results probably will be better than those of the JUA because of operating efficiencies and changes in the law that will affect claim payments. Finally, the MTF has the ability to apply for further rate relief whenever its actual financial results warrant such a request.

For all of the above reasons, only the retention of Tier II rating and the introduction of DRDP, as amended by the Commissioner, will be approved for use by the MTF at this time. However, as evidence of the Department's commitment to operate the MTF on a no profit, no loss basis, the MTF will be asked to provide quarterly statements of its financial position. Such statements will include actual current results as well as projections for future quarters.

If the MTF certifies or the Department staff determine that the actual results are significantly worse than the

previously projected values, this information will be viewed by the Commissioner as an "early warning" of a potential MTF rate deficiency. The Commissioner, upon receiving a quarterly report showing significant deterioration in the MTF financial results, will order the MTF to prepare an actuarial evaluation of its rate needs that will serve as the basis for approving an appropriate MTF rate increase.

Upon the full review by the Department of Insurance, it is ordered on this 10th day of May 1991, that:

- (1) the MTF request for the elimination of Tier II rates from its current rating program is disapproved;
- (2) the MTF request for the elimination of DIP rating is approved;
- (3) the MTF request for the introduction of DRDP rating, as amended by the Commissioner, is approved;
- (4) the MTF request for a flex rate increase is disapproved;
- (5) the MTF request for the use of a nine month, six installment premium payment plan is approved as filed on April 18, 1991; and,
- (6) all MTF new and renewal business with effective dates on or after June 15, 1991 shall be subject to rates determined according to the rating program hereinabove approved.

In addition, the MTF is ordered to provide the Commissioner with a quarterly statement of its financial position, including such operating information as income, expenses, loss payments, loss reserves, and cash flow. As the purpose of these quarterly statements is to allow the

Department and the Commissioner to monitor the financial status of the MTF, the operating statement shall include the projected values for future periods as well as the actual current period results.

This Order constitutes a final agency decision and is effective immediately. Any appeals from this Order must be filed in the Appellate Division within 45 days of the date of the Order.

DATED: 5/10/91 /s/ Samuel F. Fortunato
Samuel F. Fortunato
Commissioner

QA/mtfrat91.det

APPENDIX A

DRDP Eligibility Point Rating Factors

No. of Eligibility Points *	Rating Factor **
0	1.00
1	1.49
2	1.20
3	1.59
4	1.49
5	1.41
6	1.59
7	2.12
8	1.88
9	2.20
10	2.13
11	1.85
12	2.59
13	2.09
14	2.59
15	2.50
16	1.93
17	2.92
18	2.25
19	2.92
20	2.80
21	2.68
22 or more	2.90

* In determining the applicable rating factor, no eligibility points are assigned to at fault accidents. Flat charges for at fault accidents are imposed separately under the MTF DRDP.

** The selected rating factors produce gradual growth in the rate increase amount as the number of eligibility points goes from 1-9, considering the rates currently paid under DIP. For insureds with 10 or more eligibility points, the rate increase is the same as for those with 9 points.

APPENDIX 13

NOT FOR PUBLICATION WITHOUT THE
APPROVAL OF THE COMMITTEE ON OPINIONS
SUPERIOR COURT OF NEW JERSEY APPELLATE
DIVISION A-4634-90T5

(Filed Nov. 19, 1991)

IN THE MATTER OF THE
COMMISSIONER OF INSURANCE'S
MAY 10, 1991 ORDERS REGARDING
THE JANUARY 17, 1991 RATE FILING
BY THE MARKET TRANSITION FACILITY OF
NEW JERSEY.

The opinion of the court was delivered by
COHEN, R.S., J.A.D.

Allstate Insurance Company appeals two orders of the Commissioner of Insurance. The first is the order denying Allstate a role in the proceedings leading to the order setting auto insurance premiums of the Market Transition Facility ("MTF"). The second is the Commissioner's MTF rate order itself. Two other insurers, Aetna Casualty and Surety Company and Liberty Mutual Insurance Company, also appealed the Commissioner's rate order. A-4844-90T5 and A-5298-90T5. Their appeals were stayed on the Commissioner's motion, pending disposition of the present appeal. We reverse the order excluding Allstate from the rate-setting process and order the Commissioner to take immediate action to set proper MTF rates.

The dispute arises out of New Jersey's perennially troubled auto insurance market. The background was thoroughly explored in *State Farm Mut. Auto. Ins. Co. v. State*, 124 N.J. 32 (1991). See also *in re Assignment of Exposures*, 248 N.J. Super.

367 (App. Div.), *certif. denied*, ___ N.J. ___ (1991), and *Allstate Ins. Co. v. Fortunato*, 248 N.J. Super. 153 (App. Div. 1991). The present case requires us to review some of the history.

In 1983, the New Jersey Automobile Full Insurance Availability Act was adopted. N.J.S.A. 17:30E-1 *et seq.* Its principal purpose was to assure access to automobile insurance at standard market rates to qualified persons who could not otherwise obtain insurance. N.J.S.A. 17:30E-2. The Act replaced the assigned risk plan, created by N.J.S.A. 17:29D-1, with a new residual market mechanism, which came to be called the "Joint Underwriting Association" or "JUA," and which was to offer policies to drivers rejected by the voluntary market. In the late 1980s, despite periodic legislative efforts to provide financial relief, JUA was in deep financial trouble. Private insurers had steadily reduced their market share, and willingly covered only the best risks. JUA had to take on more and more high-risk drivers, urban drivers, young drivers and others whom the insurers, for good reason or bad, rejected. Ultimately, half of New Jersey's drivers were insured by JUA. The insurers blamed the Commissioner's refusal to permit them to charge sufficient premiums for high-risk private business. The Commissioner consistently denied rate relief. Although many of JUA's insureds were safe drivers, its population included the bulk of the State's worst risks.

JUA was required to cover risks rejected by the voluntary market, but it could charge them no more than standard market premium rates. JUA would therefore suffer losses in the absence of revenue supplements. Additional funds were expected to be raised from bad-driver and accident surcharges imposed by the Division

of Motor Vehicles and JUA, and the "residual market equalization charge" ("RMEC"), which was to be laid equally on all autos insured in the voluntary and residual markets except those with principal drivers aged 65 years or older. The RMECs were required to be periodically set by the Commissioner. *N.J.S.A. 17:30E-8a*, at a level that would permit JUA to operate on a break-even, no profit, no loss basis. *N.J.S.A. 17:30E-3o*; *State Farm, supra* 124 *N.J.* at 41-42; *In re Assignment of Exposures, supra*, 248 *N.J. Super.* at 372-373.

A number of statutory changes took effect in 1988 in an effort to reduce the cost of auto insurance generally, and to reverse the deteriorating condition of JUA in particular. The legislative goal of providing full access to auto insurance at standard rates was modified by permitting JUA to charge bad drivers 10% annual increases for four years. *N.J.S.A. 17:30E-2, -13a to -13d*. There was an optional verbal threshold for tort actions, *N.J.S.A. 39:6A-8, -8.1*, flex rating for insurers, *N.J.S.A. 17:29A-44*, an insurers' excess profits law, *N.J.S.A. 17:29A-5.6 et seq.*, an authorization for JUA to defer payments of bodily injury losses when JUA income is insufficient to meet its obligations, *N.J.S.A. 17:30E-8.1*, a multi-tier rating system for the voluntary market, reflecting the worst risks, *N.J.S.A. 17:29A-45*, and a program for the audit of JUA's servicing carriers to find, recover, and penalize any overcharges made by them to JUA, *N.J.S.A. 17:30E-17.1*.

Most importantly, the 1988 changes provided for the depopulation of JUA over four years, leaving only the least desirable risks for it to cover, *N.J.S.A. 17:30E-14*, and those would be charged self-sustaining, unsubsidized rates. Enough JUA insureds would be periodically assigned to the voluntary market to assure that it would

absorb and cover 60%, 70%, 75% and then 80% of the market during the four years of depopulation. *In re Assignment of Exposures, supra*, 248 N.J. Super. at 374. The 1988 amendments did not solve the problems.

On March 12, 1990, the Fair Automobile Insurance Reform Act of 1990 ("FAIR Act") became effective. L. 1990, c. 8. It imposed surtaxes and assessments on the private insurers and fees to be collected from doctors, lawyers and auto body shops. The proceeds were intended to pay JUA's accumulated debt of more than \$3.3 billion over a period of time. *See State Farm, supra*, 124 N.J. at 42; *Allstate, supra*, 248 N.J. Super. 153 (App. Div. 1991).

The FAIR Act also abandoned JUA as a residual market mechanism, and created MTF. MTF was to gradually take on the risks whose JUA policies expired after September 30, 1990, and was to issue its own policies for two years, until October 1, 1992. During that time, the MTF population would be reduced, if necessary by periodic assignments of risks to insurers who did not voluntarily take on their share, to 32%, 29%, 20% and, finally 10% of the market. The 10% residuum of rejected risks would be relegated to the old assigned risk plan. N.J.S.A. 17:33B-11c(5); 17:29D-1.

MTF's initial premiums were to be based on JUA's insufficient September 30, 1990 rates. However, its short revenues, unlike JUA's, would not be supplemented with RMECs, surcharges, assessments and professional fees. (RMECs and policy constants had grown to about a third of all JUA revenues.) MTF's profits and losses would be apportioned among the auto insurers. N.J.S.A. 17:33B-11d. *In re Assignment of Exposures, supra*, 248 N.J. Super. at 375.

When private insurers took on JUA/MTF risks as part of the depopulation program, they could charge them their ordinary premium rates, or, if they chose to do so, they could charge MTF rates. *N.J.S.A. 17:33B-12*. MTF rates were higher than those of many insurers, including Allstate. In May 1991, when the Commissioner was considering MTF's rates, we heard insurers' objections to the Commissioner's January 1991 depopulation order on the ground that their premiums were too low for the new business. *In re Assignment of Exposures, supra*, 248 *N.J. Super.* 367. We concluded that the insurers' opportunity to use MTF rates for depopulation business meant that they were not being forced to take on hundreds of thousands of new, higher risks at voluntary market rates.¹ We said:

Current MTF rates are higher than the current voluntary market rates of Aetna and Allstate, and, we assume, also of Colonial Penn. In addition, MTF rates will be supplemented for substandard drivers who are still eligible for assignment. The supplement may not be as great as the insurers think will be necessary, but that is very difficult to evaluate now. Moreover, MTF has already applied to the Commissioner for a 28% rate hike, approval of which would further increase premium levels. Not enough, say the insurers, pointing out that MTF has announced that its rates need a 60% increase to permit MTF to break even; insurers are entitled to earn a profit, and MTF's break-even rates are therefore inadequate by definition. [248 *N.J. Super.* at 389].

¹ Allstate was assigned some 30,000 policies in the January 24, 1991, depopulation order. It says it will be required to accept an additional 270,000 exposures to meet its remaining depopulation obligations.

We ultimately concluded:

The insurers will be able to charge the recently enhanced MTF rates to their assigned exposures. That creates a better situation than was predicted for the insurers at the time of their briefs and oral arguments. Whether it is better enough would no doubt be the subject of some disagreement. We are in no position, however, to predict whether that untested new business taken on by the insurers from MTF at untested new MTF premium rates will result in future losses so clear and significant that the insurers are entitled to protection in advance. [248 N.J. *Super.* at 390].

MTF began issuing policies and charging premiums on October 1, 1990. The FAIR Act required it initially to use JUA rates, with a few exceptions and variations. N.J.S.A. 17:33B-11c(2). The Commissioner had the authority, however, to raise rates. N.J.S.A. 17:33B-11c(3). It must have been apparent to the Commissioner, as the operator of MTF, that the JUA rates were too low. They were so low in the late 1980s that even cash flow accounting, RMECs, bad-driver increases and other revenue enhancers did not prevent dramatic yearly deficits. The anticipated greater accountability and efficiency of MTF, limitation of generous policy benefits, and other cost containment measures could be expected to accomplish just so much. The loss of RMECs would be a tremendous loss of revenue, and there were no means provided in the FAIR Act to subsidize residual market premium rates.

In November 1990, MTF received the reports of two actuarial consulting firms which had been retained to study the appropriate level of MTF rates. One firm Milliman & Robertson, Inc. ("Milliman") had been retained by the Department of Insurance itself, through MTF. The

other, William M. Mercer, Inc. ("Mercer") had been brought in by the insurance industry through the MTF Advisory Board's Actuarial Committee. (The Advisory Board is a statutory body without operational authority whose members are appointed by the Commissioner of Insurance, largely from the insurance field. *N.J.S.A.* 17:33B-11b.)

The conclusions of the two reports were quite similar. Milliman estimated that overall MTF rates were "deficient by 62.2%" on the day it opened for business: liability coverages were 97.7% low, and physical damage coverages were 6.0% low. Mercer concluded that the MTF deficiency was 58.0%, with liability coverages 88.5% low, and physical damage coverages 7.5% low.

Although the actuarial consultants both reported in the first half of November 1990 that MTF rates were grossly inadequate, the Special Deputy Commissioner of Insurance in charge of MTF did not ask the Commissioner for higher rates until January 17, 1991, when he formally submitted his "Filing for Rate Revision." The Commissioner studied the matter for another four months, and made his decision on May 10. MTF had by then been operating for more than 7 months with rates that were plainly and obviously too low. The Attorney General represented at oral argument that the only communications between the Commissioner and his Deputy on the subject were the official January 17 application for premium increases and the Commissioner's May 10 response. The reason we were given was that the Commissioner wanted to avoid the appearance of impropriety.

The Deputy did not apply for the 62% or 58% increase the actuarial consultants said was necessary. Instead, he asked for an overall additional 28%. He did

not tell the Commissioner he thought that an additional 28% would be enough to break even. Instead, he said:

The reason it is less than the indicated need is that any other amount would have required a large increase that would have impacted the clean driver.

Along with his "Filing," the Deputy sent copies of the two actuarial studies and a letter from the MTF Actuarial Committee describing the consequences of insufficient MTF premium rates. As far as we know, there were no other materials sent to the Commissioner. His review consisted of analyzing the reliability of the assumptions, methodologies, and conclusions of the actuaries. The Commissioner had no countervailing information that we know of, except what little he mentioned in his opinion.

In March, while the Commissioner was studying the materials submitted to him, Allstate applied for leave to intervene, only to file a brief urging that the requested 28% was not enough. It cited Administrative Code rules permitting interested parties to intervene in "contested cases." See *N.J.A.C. 1:1-16.1 et seq.* It said it was prepared to rely on the record provided by the actuarial reports and the January 17 letter of the Deputy; it would seek to present additional evidence only if the record was to be supplemented or expanded.

The Commissioner denied Allstate's application, but only on the day he made his rate determination. He said that there was no "contested case," and therefore Allstate's reliance on rules for intervention in contested cases was misplaced. He said that setting MTF rates was part of his authority as the operator of MTF, and was not the occasion for an adversary proceeding. He further stated

that the proposed intervention "would delay an expeditious decision," and that the MTF Advisory Board requested that there be no delay, but that Allstate's application for higher MTF rates proceed independently at Allstate's expense.

The Commissioner issued a 25-page opinion explaining his disposition of MTF's filing. The opinion first dealt with physical damage coverage premiums, which the consultants had evaluated as 6% (Milliman) and 7.5% (Mercer) too low. The Commissioner found that both evaluations were based on unrealistic assumptions about the pace of MTF depopulation. On the basis of the first six months of operation, the Commissioner found that depopulation was proceeding more slowly than the actuaries had predicted. He apparently assumed that the first drivers to leave MTF in the depopulation were the lowest risk drivers; thus, slower depopulation dampened the rise in average risk levels for the drivers still covered. Mercer shared this assumption. Milliman did not.

The Commissioner had additional concerns: Milliman's predicted loss trends of about 10% for collision and comprehensive coverages were too high; the use of JUA loss figures was misleading. At the bottom line, the Commissioner concluded that the actuaries' predicted deficiencies in physical damage premiums should be reduced to -3% for collision and 6.7% for comprehensive coverage.

The actuaries' liability coverages deficiency estimates were:

	MERCER	MILLIMAN
Bodily Injury	77.5%	93.9%
PIP	177.0%	173.0%
Property Damage	35.5%	31.2%
Overall	88.5%	97.7%

The Commissioner concluded that these numbers were too high because depopulation was slower than expected, because Milliman's loss trend rates were too high, and because MTF proposed certain changes that would cost money and which the Commissioner had disapproved.² The Commissioner stated that the actuaries' predictions had to be adjusted for their forecasting inaccuracies. Without identifying the magnitude of the inaccuracies, he reduced the overall Mercer estimate from 58% to 51.5% and Milliman's from 62.2% to 43.3%. The average of the two was 47.4%.

The rating plan which the Commissioner approved would produce an 18.6% increase in MTF revenues. Adjustments in the rating plan would produce further revenues which the Commissioner did not estimate, but he ultimately recognized that the actuarial evaluations appeared to indicate the need for an additional 24.3% to break even. He then commented:

Critics of this decision probably will use the two MTF actuarial studies to claim that the Department has underfunded the MTF deliberately. There are several reasons, however, to question whether the actuarial estimates of the MTF rate needs are accurate.

Again, the Commissioner questioned the use of JUA data to forecast MTF results: lower benefit payouts could be anticipated, along with more efficient operations and lower costs resulting from differences in the mix of JUA

² The relevance of this information is not clear, since the actuaries did not base their November 1990 projections on changes MTF proposed in January 1991 for adoption some months later.

and MTF insureds in the smaller share of the insured population covered by MTF. The Commissioner did not say why the smaller share should result in lower-than-anticipated deficits. Indeed, if the smaller share results from early depopulation of the better drivers, as he earlier posited, the smaller share would have a greater component of higher risks.

Finally, the Commissioner expressed his Department's "commitment to operate one MTF on a no profit, no loss basis," and stated that MTF had "ample time to make another rate application . . . if its financial results are as poor as the actuaries are predicting." He continued:

If the MTF certifies or the Department staff determine that the actual results are significantly worse than the previously projected values, this information will be viewed by the Commissioner as an "early warning" of a potential MTF rate deficiency. The Commissioner, upon receiving a quarterly report showing significant deterioration in the MTF financial results, will order the MTF to prepare an actuarial evaluation of its rate needs that will serve as the basis for approving an appropriate MTF rate increase.

The Commissioner therefore told MTF to provide him with quarterly statements of its financial position, including actual current results as well as projections for future quarters, showing income, expenses, loss payments, loss reserves, and cash flow.

Evaluation of the Commissioner's rate order and refusal to let Allstate participate has to include an

analysis of the differences between MTF and its predecessor, JUA. JUA was an unincorporated non-profit association of all New Jersey auto insurers. *N.J.S.A.* 17:30E-4. It had a board of directors of 17 members,³ 14 appointed by the Governor, one each by the President of the Senate and the Speaker of the Assembly, and, *ex officio* the Director of the Division of Motor Vehicles. The insurance industry was well represented on the Board, *N.J.S.A.* 17:30E-5a. It was to adopt a plan of operation, subject to the Commissioner's approval. *N.J.S.A.* 17:30E-6. JUA was granted broad operating authority, to be exercised by the Board and a general manager who reported to the Board and not to the Commissioner.⁴ *N.J.S.A.* 17:30E-7. The Board was sufficiently independent to litigate with the Commissioner over the imposition of RMECs. See *New Jersey Auto. Full Ins. Underwriting Ass'n v. Gluck*, No. A-4870-84T1 (App. Div. June 19, 1986). JUA's sources of income have already been described, as has its express obligation to operate on a break-even basis by the exaction of sufficient RMECs from the policyholders. The insurers were not responsible for JUA losses.

The JUA statute has a detailed provision for mandatory hearings to be conducted by a panel of the Board on the request of a member insurer aggrieved by a ruling of JUA, or its failure to adhere to its plan of operation, or to the enabling statute. The Board's ruling was appealable

³ Later reduced to 9 members. *L.* 1988, c. 119, § 17.

⁴ In 1986, the Legislature declined to enact a proposed amendment to have the general manager report to the Commissioner instead of the Board.

to the Commissioner and then to this court. *N.J.S.A.* 17:30E-16.

MTF's statute is different. *N.J.S.A.* 17:33B-11 creates MTF, "to be operated by the Commissioner of Insurance pursuant to the provisions of this section." It does not describe MTF as an unincorporated non-profit association of auto insurers or any other kind of entity. It merely says the auto insurers shall be members of MTF "and shall share in its profits and losses." *N.J.S.A.* 17:33B-11a. There is no board of directors or general manager reporting to it, but only an advisory board. *N.J.S.A.* 17:33B-11b. There is no express provision for rate subsidies or break-even operation, or for hearings at the request of an aggrieved insurer. There is no person or board empowered to confront the Commissioner regarding MTF operations.

JUA was structured as an entity with a chief executive and board of directors who functioned somewhat independently. The consumers' and the insurers' interests were protected by representation on the Board. Premiums were set by the voluntary market. The Commissioner had ultimate financial control because the imposition of RMECs was his responsibility. He had the obligation, however, to set the RMECs high enough to cause JUA to operate on a no profit, no loss basis. *N.J.S.A.* 17:30E-30. The point is that, with that very significant exception, JUA was not the Commissioner's direct responsibility.

MTF, on the other hand, is the Commissioner's operation. He may, of course, designate subordinates for day-to-day functions. The Commissioner is not, however, a neutral sometime referee for an insurance mechanism

operated by others. As the Commissioner said in rejecting Allstate's motion to intervene:

The Legislature directed that the MTF is "to be operated by the Commissioner. . . ." Thus the determination fixing rates for MTF is a matter solely within the scope of the Commissioner's powers.

The other salient difference between JUA and MTF is the matter of deficits. The Legislature told the Commissioner to see to it that JUA broke even. It did not contemplate that he would not do so; it provided no means to pay a deficit. Only later, after JUA ran up a \$3.3 billion deficit, was legislation enacted to deal with it.

The FAIR Act does not expressly require MTF to be a break-even operation, but the law cannot be otherwise. If there were no such requirement, the Commissioner could purposely set rates high enough to yield a profit, which he could then distribute to the member insurers. There is, however, nothing in the text or purpose of the FAIR Act that entitles the Commissioner to operate MTF to make a profit. It is unthinkable, not only as a matter of policy but also as a matter of law, that the Commissioner might plan such a windfall for insurers at the expense of policyholders.

It is equally unthinkable to suggest that the Commissioner could decide, as a matter of policy, to select deficit rates, and later send apportioned bills to the member insurers. The statute does not expressly confer such a power to tax the insurance companies. There is no

obvious method for them to pass the cost on.⁵ The Commissioner did not argue in his May 10, 1991 opinion or before us on appeal that he has such authority. Indeed, he expressed his "commitment to operate the MTF on a no profit, no loss basis. . . ."

When the Legislature wanted to impose financial burdens on the insurance companies in the FAIR Act, it knew how to do so in plain terms. For example, it levied assessments and surtaxes designed to pay off JUA's accumulated debt. *N.J.S.A.* 17:30A-8a(9) and (10), 17:33B-49. The assessments cannot be passed along, dollar for dollar, to the policyholders. *N.J.S.A.* 17:30A-16b. Also, the Commissioner is to ensure that policyholders do not pay for the surtax. *N.J.S.A.* 17:33B-51. In *State Farm*, the Supreme Court read the FAIR Act to bar direct pass-throughs of assessments and surtaxes, but said they were not unlawful on their face, on the assumption that the Commissioner would fulfill his duty to see to it that the insurers would receive a constitutionally fair overall rate of return, see *Sheeran v. Nationwide Mut. Ins. Co., Inc.*, 80 N.J. 548, 560 (1979), and that he would act in a realistic and timely manner consistent with that statutory duty. *State Farm, supra*, 124 N.J. at 62-63.

The Commissioner does not make the argument that prevailed in *State Farm*. He does not contend that the statute authorizes him to run MTF at a loss to the

⁵ We were told at oral argument that the Commissioner does not plan to send bills to the insurers until 1993. It is not clear exactly how they would be able to recoup the expenses at that late date.

insurers; with the insurers' right to a fair return authorizing them to pass along the costs only if necessary to prevent an unconstitutional taking. In his opinion, the Commissioner expressed his "commitment to operate the MTF on a no profit, no loss basis." In his brief before us, he describes his "dedication" to that proposition "in fulfillment of his perception of the legislative intent."

The question before us is not the one decided in *State Farm*. There, it was clear that the Legislature had imposed financial burdens on the insurers, and the Supreme Court had to determine the constitutionality of the imposition. Here, the question is whether the Legislature, by saying that the insurers share MTF's profits and losses, but without any operating role, has authorized the Commissioner to set MTF rates at a loss-producing level. Although he does not argue that he has that authority, it is useful to rule clearly that he does not.

We defer to reasonable exercises of administrative agency expertise. *Henry v. Rahway State Prison*, 81 N.J. 571, 579-80 (1980). We recognize the Insurance Department's familiarity with the operations of the auto insurance market. *IFA Ins. Co. v. New Jersey Dep't of Ins.*, 195 N.J. Super. 200, 206-07 (App. Div.), *certif. denied*, 99 N.J. 218 (1984). We do not have to deal, however, with a contested agency interpretation of its enabling statute. See *Smith v. Director, Div. of Taxation*, 108 N.J. 19 (1987). And that is because the Commissioner's view coincides with Allstate's and our own: his duty is to operate MTF on a break-even basis. We repeat that there is no disagreement on that score, and no contention that the insurers must pay up and hope for later rescue in a constitutional safety net.

When the Commissioner sets MTF rates, it is not necessary for him to act as a neutral adjudicator of his Deputy's presentations or even of cases made by opposing parties. That is the Board-of-Public-Utilities model, and it does not fit very well. The Commissioner is the chief executive and operating officer of MTF, and he chose a Deputy to run it on a daily basis. The Commissioner surely has no need to avoid discussing rates with his Deputy to avoid the appearance of impropriety. The Deputy is his subordinate, and runs MTF in his name. That does not mean, however, that the Commissioner may set MTF rates in a closed-door process from which those affected are completely excluded.

The March 12, 1990 statute directed the Commissioner to adopt procedures for "the filing and approval of changes in [MTF] rates . . . " N.J.S.A. 17:33B-11c(3). He did not do that. If he had done so, he might have followed the BPU model, at least to the extent of erecting the framework for an adversary process that included plenary presentation of evidence. He might instead have followed the rule-making model, in which he would have published proposed rates and subjected them to public scrutiny and comment by affected parties before deciding whether to adopt them. See *State, Dep't of Env'tl. Protection v. Stavola*, 103 N.J. 425 (1986); and Justice Handler's dissent, *id.* at 439; *Metromedia, Inc. v. Director, Div. of Taxation*, 97 N.J. 313 (1984). We call the Commissioner's attention to *Bally Mfg. Corp. v. New Jersey Casino Control Comm'n*, 85 N.J. 325 (1981), *appeal dismissed*, 454 U.S. 804, 70 L. Ed.2d 74 (1981), and particularly to Justice Handler's concurring opinion, *id.* at 337.

The intersection between agency adjudication and rule-making functions is, as the cited cases show, not always an easy one to locate. It is not for us to make an initial determination whether one process or the other is more suitable, or even exclusively suitable, to deal with MTF ratemaking. What can safely be said, however, is that some process must be devised and employed that will take adequate account of the fact that MTF rate-making decisions dispose of hundreds of millions of dollars of somebody else's money. Such decisions cannot be made behind closed doors, out of the sight of the people affected and without the benefit of any input from them.

Since the Commissioner did not follow the statutes's direction to adopt procedures for MTF ratemaking, we have no opportunity to evaluate adopted procedures. It would, however, be inappropriate for us to select a particular path for the Commissioner to follow. There are many possibilities, and it is for him to choose among them. The problem is that time is passing rapidly and, perhaps, irretrievably.

In his May 10 rate order, the Commissioner said that monitoring actual MTF operations would permit him to see if the actuaries' forecasts were accurate or, as he then believed, unduly pessimistic. If they were accurate, he could consider raising MTF rates. It is now thirteen months since MTF opened for business, and six months since MTF's rates were raised 18.6%. The first quarterly report the Commissioner asked his Deputy for will not, we are told, be ready until late December. And, that is not a firm date. We are not intimately familiar with the Department's records of MTF operations. We are unaware, however, of any actions being taken by the

unaware, however, of any actions being taken by the Commissioner to test the validity of his May 10 skepticism regarding the actuaries' forecasts. It is apparent that an immediate and assiduous search for guidance in the available records of MTF experience would enable the Commissioner to better evaluate his May 10 forecasts and the actuaries', and to make appropriate plans for the future.

The Commissioner is faced not only with the possibility of creating tremendous MTF losses by permitting operations at insufficient rates, but also the possibility of creating additional losses for private insurers on voluntary business written at MTF rates for depopulated risks. And yet, the timetable he set in his May 10 order for "early warning" of potential deficits depended on quarterly reports from MTF, the first one of which is not expected to be complete until late December. Then, the Commissioner may order MTF "to prepare an actuarial evaluation of its rate needs", and then a rate increase will be considered. The problem, of course, is that the time for charging increased premiums grows shorter every day, and will soon disappear altogether. We note that the Commissioner had the duty to approve or disapprove a JUA filing for increased RMECs within 60 days. Inaction constituted an approval. N.J.S.A. 17:30E-8b.

Rate hikes are prospective only. *In re Petition of Elizabethtown Water Co.*, 107 N.J. 440, 452-60 (1987). There is no way for MTF or voluntary market insurers to charge retroactively higher premiums for earlier policy periods. Thus, the continued inadequacy of MTF rates, if indeed they are inadequate, would constitute a continually increasing loss that could never be made up. In these

circumstances, all practical speed is the only acceptable pace for appropriate proceedings for review and evaluation of MTF rates. It may not be possible to make definitive judgments about MTF's predicted losses, but there are enough problem indications to require the Commissioner's immediate attention. He must determine if losses are and will be sustained at present premium levels. If so, he must determine what increases to direct in order to operate MTF on a breakeven basis. The Commissioner can not responsibly wait for sufficient information to be absolutely sure. If he were operating MTF with public funds, it would be unthinkable for him not to keep a constant eye on the bottom line. He owes no less to the insurance companies.

We have considered denying any present relief, and relegating the insurers to whatever defenses they may later assert if the Commissioner bills them for MTF losses. Since the bills would come so late in the day, the result of relieving insurers of their burden would be serious. The legislation contemplates no alternate source of MTF subsidy. The question whether MTF is something other than a part of the Insurance Department, financed by general tax revenues, would obviously be a focal issue.

We suggest no answers to any of these questions. In particular, we do not say whether the insurers could avoid MTF bills if they could prove that the Commissioner knowingly ran MTF at a loss, or what the alternate source of funds would be. We say only that there are no happy answers to such questions, and that only immediate attention by the Commissioner can lessen their impact.

We also express no opinion on the Advisory Board's suggestion that Allstate could independently and at its own expense apply to the Commissioner for an MTF rate increase. It has not attempted to do so, and we have no occasion to deal with the possibility.

The manner of proceeding to consider and determine MTF rates will forthwith be chosen by the Commissioner. The proceeding must afford interested parties a voice and reasonable advance access to the relevant information in the hands of the Department of Insurance. The Commissioner must act speedily. Proceedings conducted at a leisurely pace can consume many months and confirm the insurers' suspicion that the Commissioner is in no hurry to look realistically at MTF rates. Recognition of the fact of regulatory lag will excuse only delay that is absolutely unavoidable. *Helmsley v. Borough of Fort Lee*, 78 N.J. 200, 226-30 (1978), *appeal dismissed*, 440 U.S. 978 (1979).

We order the Commissioner to meet with representatives of interested parties⁶ within 15 days of this opinion to fix a manner and a time schedule for the accomplishment of the purposes identified in this opinion. We expect him to establish a brief timetable for preparation, a forthcoming response to legitimate demands for relevant Department records, and a procedure suited to the protection of the rights of all interested parties.

⁶ Policyholders are also interested parties. Perhaps the Public Advocate might represent them. See N.J.S.A. 52:27E-18. The authority of the Division of Rate Counsel seems broad enough to include such an undertaking.

APPENDIX 14
STATE OF NEW JERSEY
DEPARTMENT OF INSURANCE

December 4, 1991

CN 325
TRENTON 08625-0325

Honorable Samuel F. Fortunato
Commissioner of Insurance
State of New Jersey
Department of Insurance
20 West State Street
CN 325
Trenton, New Jersey 08625-0325

Dear Commissioner Fortunato:

I am submitting for your review and approval a filing for an interim rate increase for the Market Transition Facility (MTF).

After consulting with the MTF Advisory Committee, it is their recommendation that we file for a 22 percent increase on liability coverages, which will result in an overall increase of 15 percent. The liability increase would be as follows:

Bodily Injury	+ 11.2%
Property Damage	+ 5.4
Personal Injury Protection	+ 70.4
Total	<u>22.0%</u>

The MTF will soon have fiscal year end figures including IBNR. At that time a true rate indication will be developed. The Committee has requested that I file another request for the full rate indication.

Very truly yours,

/s/ R. T. Haskins

R. T. Haskins, CPCU, CLU
Special Deputy Commissioner
Market Transition Facility

cc: Public Advocate

Rate Proposal
New Jersey Market Transition Facility

I. INTRODUCTION

The New Jersey Market Transition Facility retained the services of O'Neil Consulting Services to develop an estimate of the maximum possible range of its overall rate level needs. The results of that analysis are summarized in the attached report.

It should be noted that the analysis was completed in an expedited time frame and, therefore, includes a number of limitations as identified in the report.

The purpose of this memorandum is to propose a +15.0% overall rate level change (or increase in income) effective January 15, 1992.

The distribution of the proposed change is described in the next sections.

II. DISTRIBUTION OF OVERALL RATE LEVEL CHANGE

The proposed +15.0% rate level change would be distributed entirely to the liability coverages and then to individual coverage in proportion to the indicated midpoint

rate level changes. The proposed changes by coverage are shown on the attached Exhibit A.

III. EFFECT OF UNMET-DEPOPULATION QUOTAS ON MTF RESULTS

It should be noted that some of the current MTF loss is due to the unmet depopulation quotas. Specifically, the MTF currently insures 294,000 cars more than expected at this point in time. Exhibit B displays the dollar impact on MTF results of this unmet quota, assuming that, (1) all of these risks had the same distribution of clean/surcharged as the MTF overall, (2) there was no loss ratio differential between the clean/surcharged risks, and (3) the written premium and earned premium are distributed in proportion to the number of risks. None of these assumptions is very likely to hold. However, they produce a baseline estimate. Deviations from the assumptions, a larger proportion of clean risks in the depopulation pool versus the total market, and a loss ratio differential, result in reductions in the dollar impact of unmet depopulation quotas. Exhibit B page 2 provides an estimate of the dollar impact for various combinations of assumptions regarding the proportion of clean risks in the depopulation pool and the loss ratio differential between clean and surcharged risks. In sum, these calculations suggest that between \$50 and \$147 million of the MTF loss is due to unmet depopulation quotas.

Exhibit A

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New Jersey - MTF

Private Passenger Automobile Statewide Rate Review
Summary of indicated and Proposed Rate Level ChangesI. Percentage Effects

<u>Coverage</u>	<u>EP (000)</u>	<u>Proposed Overall Rate Level Change</u>
Bodily Injury and UM	\$268,569	11.2%
Property Damage	\$137,011	5.4%
PIP	\$106,603	70.4%
Liability Subtotal	\$512,183	22.0%
Comprehensive	\$ 92,312	0.0%
Collision	\$145,537	0.0%
Physical Damage Subtotal	\$237,849	0.0%
All Coverages	\$750,032	15.0%

II. Dollar Effects on Written Premium (000)*

<u>Coverage</u>	<u>WP (000)</u>	<u>Proposed Overall Dollar Effect</u>
Bodily injury and UM	\$ 428,690	\$ 47,904
Property Damage	\$ 222,057	\$ 12,022
PIP	\$ 200,363	\$141,108
Liability Subtotal	\$ 851,109	\$201,033
Comprehensive	\$ 136,734	\$ 0
Collision	\$ 234,847	\$ 0
Physical Damage Subtotal	\$ 371,580	\$ 0
All Coverages	\$1,222,690	\$201,033

* Written premium shown is for eleven months. Annual dollar effects would be 9.1% greater. Note also, however, that the effective date of 1/15/92 provides for collection of premium at the new rate for only eight and one half months or 70% of the annualized amount. Therefore, 77.3% of the amount shown would be realized additional income.

Exhibit B

Page 1

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New Jersey - MTF

Private Passenger Automobile Statewide Rate Review
 Estimated Effect of Unmet Depopulation Expectations

Number of Undepopulated Risks 294,000
 % Share of MTF Liability Written
 Exposure thru 8/31/91 22.3%

Adjusted Percentage Indications*

<u>Coverages</u>	EP (000)	<u>Range of Indicated Rate Level Changes*</u>				
		LOW POSSIBLE	LOW PROBABLE	MIDPOINT	HIGH PROBABLE	HIGH POSSIBLE
Bodily injury and UM	\$208,571	6.3%	15.2%	24.0%	32.8%	41.6%
Property Damage	\$106,403	-1.4%	6.1%	11.0%	18.1%	84.8%
PIP	\$ 82,758	104.3%	127.0%	151.2%	174.0%	198.0%
Liability Subtotal	\$397,761	24.7%	35.9%	47.1%	58.4%	86.8%
Comprehensive	\$ 71,669	3.1%	6.7%	10.0%	13.3%	17.4%
Collision	\$??3,024	-10.9%	-7.3%	-0.7%	-0.1%	3.5%
Physical Damage Subtotal	\$164,713	-6.5%	-1.9%	1.7%	8.0%	8.9%
All Coverages	\$582,476	15.1%	23.9%	32.7%	41.8%	50.4%

* Estimates were made only for the low possible, midpoint, and high possible points of the range. The others may be interpolated. These estimates assume: (1) the written premium and earned premium are proportional to the number of risks; (2) the risk would have been removed uniformly from all MTF risk categories; (3) the loss ratio for all the categories is the same.

II. Adjusted Dollar Effects of the Indications on Written Premium*

<u>Coverage</u>	<u>WP (000)</u>	<u>Range of Indicated Dollar Effects (000)**</u>			<u>Difference From Current Estimated Range of Indicated Dollar Effects (000)**</u>		
		<u>LOW POSSIBLE</u>	<u>MIDPOINT</u>	<u>HIGH POSSIBLE</u>	<u>LOW POSSIBLE</u>	<u>MIDPOINT</u>	<u>HIGH POSSIBLE</u>
Bodily injury and UM	\$352,920	\$ 21,074	\$ 79,555	\$134,806	\$ 6,062	\$22,071	\$ 59,391
Property Damage	\$172,440	(\$ 2,498)	\$ 20,041	\$ 42,459	(\$ 693)	\$ 5,766	\$ 12,223
PIP	\$165,602	\$162,343	\$238,228	\$508,107	\$48,700	\$67,003	\$ 00,031
Liability Subtotal	\$660,972	\$181,009	\$332,120	\$489,232	\$ 2,070	\$00,402	\$140,738
Comprehensive	\$108,188	\$ 0,297	\$ 10,911	\$ 18,526	\$ 948	\$ 3,100	\$ 5,328
Collision	\$182,382	(\$ 18,874)	(\$ 6,789)	\$ 7,355	(\$ 6,717)	(\$ 7,777)	\$ 1,629
Physical Damage Subtotal	\$200,509	(\$ 10,577)	\$ 4,153	\$ 24,552	(\$ 4,755)	\$ 1,188	\$ 7,158
All Coverages	\$949,541	\$164,432	\$339,273	\$614,114	\$47,331	\$97,597	\$147,592

** Written premium shown is for eleven months. Annual dollar effects would be 9.1% greater. Note also, however, that the effective date of 1/15/82 provides for collection of premium at the low rate to only eight and one months of 70% of the annualized amount. Therefore, 17.3% of the amount shown would be realized additional income.



Exhibit B

Page 2

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Private Passenger Automobile Statewide Rate Review
 Estimated Effect of Unmet Depopulation Expectations
 Estimates Based on Varying Assumptions

Assumed % Clean of Depop Risks***	Loss Ratio Range****	Overall Dollar Effect on MTF Indicated Rate Requirements (000)*			
		Loss Ratio Differential Surcharged/Clean**			
		<u>1</u>	<u>1.1</u>	<u>1.25</u>	<u>1.5</u>
64.4%	Low	\$ 47,301	\$ 47,301	\$ 47,301	\$ 47,301
	Mid	\$ 97,597	\$ 97,597	\$ 97,597	\$ 97,597
	High	\$147,892	\$147,892	\$147,892	\$147,892
80.0%	Low	\$ 47,301	\$ 44,020	\$ 39,500	\$ 32,878
	Mid	\$ 97,597	\$ 93,365	\$ 87,535	\$ 78,994
	High	\$147,892	\$142,909	\$138,045	\$125,989
100.0%	Low	\$ 47,301	\$ 39,613	\$ 29,499	\$ 14,387
	Mid	\$ 97,597	\$ 87,939	\$ 74,636	\$ 56,145
	High	\$147,892	\$136,621	\$120,857	\$ 97,907

* MTF dollar requirements would be less to the extent shown had depopulation of the 294,000 risks taken place.

** The loss ratio differential has no effect when the proportion of clean risks in the depopulation pool is the same as for the original pool.

*** The proportion of clean risks in the depopulation pool has no effect when the rate differential is 1.0.

**** Only the low possible, midpoint, and high possible points of the range are shown. Values for the others may be interpolated.

New Jersey Market Transition Facility
Report of Rate Level Indication Analysis

I. INTRODUCTION

O'Neil Consulting Services was retained by the New Jersey Market Transition Facility (MTF) to calculate the maximum possible range of its indicated rate level requirements. This report outlines the data, assumptions and methodologies underlying the requested calculation.

This report was prepared in an expedited time frame. Therefore, some of the procedures employed were modified or adapted from other studies completed for the MTF. These areas are noted as applicable in this report.

This report is organized into the following sections: background, conditions and limitations, results, data, and assumptions and methodologies.

II. BACKGROUND

The MTF was created by Section 88 of the FAIR Act and became operational on October 1, 1990. This operational date was coincident with the date after which the JUA (AFIUA) was prohibited by the FAIR Act from issuing or renewing automobile insurance policies. The MTF is a temporary market mechanism designed to facilitate the transition of "eligible" drivers, as defined in the FAIR Act and attending regulations, from the JUA to coverage in the voluntary market. The MTF has only a two year life span. Under the FAIR Act, the MTF was initially authorized to charge the JUA rates. On January 17, 1990, the MTF filed a request for an overall increase in rates with the Commissioner. On May 10, 1991, the Commissioner

granted an overall 18.6% premium increase to the MTF, effective June 15, 1991.

III. CONDITIONS AND LIMITATIONS

The analysis herein was based on the data and information provided by the MTF. No independent audit or verification of the data/information was completed. To the extent such data/information was either inaccurate or incomplete, the results derived therefrom will also be inaccurate, incomplete, and/or biased. To the extent possible, areas of such deficiency were identified and discussed.

Further, this analysis projects loss and expense costs into a prospective rating period. All such projections are estimates and may err due to various unforeseeable contingent events. These include, for example, additional law changes, changes in regulation, or changes in policy/claim handling procedures.

The ranges of indications included herein were completed at the request of the MTF. OCS makes no representation that the maximum possible range of indicated rate level need discussed herein is appropriate. The limitations of these estimates are discussed further in the results section below.

Finally, as noted above, this report was prepared on an expedited basis. Accordingly, the methodologies used contained assumptions and limitations which might be more explicitly considered in a more detailed study. Specifics of these limitations are discussed in the applicable

sections of this report. These are listed here for reference, as well, without explanation.

1. All calculations were completed as if the MFT were an on-going operation. Trend periods, etc. are fully included for both income and outgo.
2. No adjustment was made to provide for the incomplete policy term available for collection of the required rate.
3. All calculations are prospective. No consideration was given to recoupment for possible past losses.
4. Investment income was estimated in a standard manner. No consideration was given to the fact that funds may not be available for investment if they must be used to pay for prior period losses.
5. No attempt was made to quantify or evaluate potential changes in the size or mix of the MTF book of business.
6. No attempt was made to adjust the data for distortions due to start-up of the MTF such as the lag in earned premium or paid loss.
7. On-level premium was calculated at full value based on the +18.6 rate change, despite the fact that that amount was not realized by the MTF.
8. The one time start-up costs of \$5.6 million and other minor miscellaneous expenses were not explicitly included in the calculation.
9. IBNR was estimated without a detailed study.

IV. RESULTS

There were numerous variables underlying the analysis of the MTF rate level level need. Most of these variables lie within a range of the correct result. In this case, the most significant unknown factor was the quantification of the MTF IBNR. Therefore, as requested by the MTF, the range of results was determined thru variations in the selected IBNR factor. OCS calculated the probable range of MTF rate level requirements at +24% to +42%. At the request of the MTF, a maximum possible range was also calculated. This resulted in a maximum possible range of overall indicated rate level need from +15% to 50%. The midpoint of both ranges was +32.7%. The credibility of these results is greatest at the midpoint and decreases as the range diverges in either direction to the point of *essentially zero credibility at the endpoints of +15% and +50%.*

Therefore, although the maximum possible range is from 15% to 50%, it is OCS's opinion that the *maximum probable range is from 24% to 42% with the most probable result at 32.7%. The results of the maximum possible range should be viewed with extreme caution. Implementation of a rate change less than the probable range would be, based on the information currently available, actuarially unsound and likely result in an MTF deficit.*

Results by coverage are shown on Exhibit 1.

The effective date underlying the indicated rate level changes is 1/15/92.

V. DATA

The underlying data were taken primarily from monthly summaries of operations provided to the MTF by AIPSO. The data are by policy year and accident year from inception of the MTF, October 1, 1990, thru August 31, 1991, a period of eleven months. Data elements provided were extensive and included, income items: written premium, earned premium, written DIP/DRDP, earned DIP/DRDP, and outgo items: paid loss, outstanding loss, UCJF recoveries, paid ale, directly reimbursable expenses, SIU expenses, claim service fees, non-claim service fees, and commissions written.

Data were also obtained from a variety of other sources. Administrative costs, premium taxes, and the expected UCJF assessment were estimated from the MTF Financial Statements.

VI. ASSUMPTIONS AND METHODOLOGY

The assumptions and methodology associated with each step of the calculation are described below.

A. Income Items.

1. Written Premium

DIP/DRDP written premium was available only for liability as a whole. For purposes of determining the required rate level by coverage, DIP/DRDP written premium was apportioned to each liability coverage based on the proportion of each coverage's written premium to total liability written premium.

2. Earned Premium

Earned premium by coverage was estimated because neither earned nor unearned premium were available by coverage for the non-quarter ending month of the experience period (August). The estimate was completed by allocating the total liability unearned premium at August to coverage based on the known proportion at June. The same procedure was applied to the physical damage coverages.

Unearned premium was allocated to DIP/DRDP in a similar manner. The resulting DIP/DRDP earned premium was then allocated to coverage in proportion to earned premium.

3. Earned Premium at Current Rates/Premium Trend

Effective June 15, 1991, the MTF was granted an 18.6% premium increase in the form of the DRDP rating factors and increased flat dollar accident surcharges. The factors utilized by the DRDP apply to all coverages except PIP while the flat dollar accident surcharges relate to all coverages. Accordingly, the effect of the 18.6% rate level change was apportioned to DRDP and the effect of the increased accident surcharges. This computation resulted in premium effects of 20.8% for all coverages except PIP and 8.3% for PIP. An on-level adjustment factor was developed using the parallelogram method and applied to all coverages. The on-level factors were 1.202 for all coverages except PIP and 1.081 for PIP.

It should be noted that the +18.6% premium change resulted from changes in rates only for risks with one or

more points. The estimated value of the premium change was based on the assumption that 59% of MTF insureds would have one or more points. The actual figure has been about 36%. Therefore, the value of the last MTF rate level change was overstated. Nonetheless, the full value was included herein.

Physical damage coverages were also adjusted to provide for model year rating and symbol drift. Due to time constraints, the factors developed in the Mercer draft report of July 12, 1991 were used. These were, 14.1% for comprehensive and 9.9% for collision.

Due to start-up of the MTF operation, earned premium is probably somewhat understated relative to a going concern operation. No attempt was made to adjust for this observation.

The understatement in earned premium due to start-up offsets against the overstatement resulting from the on-level factor estimate. No attempt was made to quantify the extent of this offset.

4. Investment Income

Investment income was incorporated into the permissible loss ratio by applying a cash flow approach to the other income/expense items. This method and its various parameters is described in a later section. The interest rate used for discounting was 5%, about the level of current MTF earnings.

It would be noted that no consideration was given to the fact that funds anticipated in this model may not be

available for investment if they must be used to pay prior period losses.

5. Premium Installment Fees

The total amount of such fees thru August was not available for this report. The amount thru July was just under \$9 million. Therefore, the estimated eleven month amount was \$10 million. This amount was included as an add-on to the otherwise calculated on-level earned premium. It was distributed to coverage in proportion to written premium.

B. Losses

1. Paid Loss, Outstanding Loss, IBNR

Paid loss was taken from the AIPSO reports for the first eleven months of the MTF operation. PIP was net of UCJF recoveries and comprehensive and collision were net of salvage and subrogation.

Brief review of these data suggest that the BI paid loss is experiencing a payout lag which exceeds the start-up lag of the AFIUA based on the observed level of paid loss to date. A similar lag was also observed for outstanding loss.

Because there was insufficient time to complete a full study of the required MTF IBNR, a factor was developed to reasonably approximate this value. First, the eleven months of actual MTF data were developed to 12 months using the observed month-to-month outstanding and cumulative paid history of the MTF. These data are shown on Exhibit 6.

Then development factors from 12 months to ultimate were derived using the AFIUA incurred loss development data for accident year 1984 as provided in the Milliman & Robertson 12/21/90 AFIUA reserve study. The AFIUA 1984 data were used in an attempt to recognize the start-up lag. The 11-12 month and 12 month to ultimate factors were combined to yield indicated IBNR factors by coverage.

Given the uncertainties associated with setting IBNR reserves generally, and the additional uncertainties in the New Jersey market, a range of development factors to ultimate was selected. The selected range for BI was adjusted upward in an attempt to somewhat adjust for the perceived understatement in observed payouts to date. Therefore, the low end of the range exceeds the indicated factor. The selected range around the midpoint was plus or minus 16.7%. PIP was viewed as similarly variable with a range of plus or minus 21%. The selected ranges for the remaining coverages were narrower, given their lesser expected variability. As for the rate level indications in total, the midpoint is the most credible estimate, with credibility decreasing as the figures diverge from the midpoint to essentially zero at the endpoints. The maximum probable range arises from selection of loss development factors midway between the low possible and midpoint, and high possible and midpoint.

The final selected factors are displayed on Exhibit 6.

2. Loss Trend

Because there have been numerous law changes over the last several years, trend data are sparse to non-existent.

Therefore, a combination of data sources and judgment was relied on in selecting trend amounts. These included Fast Track thru June for New Jersey, New York (BI only), and Countrywide, various CPI cost indices, and internal ISO trend data for PD. The selected amounts are described by coverage below.

a. Property Damage

For property damage severities, New Jersey Fast Track data were relied on with reference to various CPI indices which relate to automobile repair labor and parts costs. Indices related to labor were around 3% while indices related to parts costs were declining slightly.

New Jersey Fast Track data thru 6/91 has shown declining trends for both frequency and severity. The severity trend indications were +9.3, +6.2, +3.5, and +0.8, for the last 19, 12, 9, and 6 quarters, respectively. Given these trend indications and the CPI indices, a conservative severity trend of 7% was selected.

For frequency, the Fast Track data also indicated continuing declining trends. The indications were -4.5, -6.1, -7.2, and -8.5, respectively for the last 19, 12, 9, and 6 quarters. Therefore, a very conservative trend of -5.0% was selected.

It should be noted that the declining frequencies and severities observed in the New Jersey Fast Track data are corroborated by similar movement in the countrywide Fast Track indications. These are displayed on Exhibit 4 for reference.

These selections produce a pure premium trend of 1.7%.

ISO furnished the MTF with trend data thru June, 1991 for voluntary and residual market business combined and for residual market business alone. These data have two basic inherent difficulties as follows: (1) ISO did not collect data for the AFIUA (residual market) for all carriers until second quarter 1989, (2) one of the servicing carriers (CSC) has not reported claim count information to ISO. The first difficulty distorts trend indications based on more than 5 points (from June, 1990 to June, 1991). The second difficulty was eliminated by ISO's estimate of CSC claim counts. No independent review of these estimates was made.

The five point exponential pure premium indications based on the ISO data were +1.0% for total market data, and +0.2% for residual market data. These indications are consistent with the Fast Track indications and CPI indications discussed above, as well as with the selected +1.7% pure premium trend.

A summary of the indicated and selected frequency and severity trends is shown on Exhibit 4 pages 1 and 2.

b. Bodily Injury

Because of the changes in the no-fault threshold over the last seven years, New Jersey BI trend data are not meaningful as a reference in selecting trends. Further, separate frequency and severity trends are required in order to accurately reflect the anticipated environment.

Severity trends were selected with reference to the various CPI Medical Care Cost data and actual cost experience in New York. The CPI data indicate that costs are

increasing at about 7% per year for services (specifically, 5.4% for Physician's Services and 8.6% for the Medical Care Cost Index) and at about 9% to 10% for hospital costs (specifically, 9.5% and 10.8% for Hospital Rooms and Outpatient Hospital, respectively). The actual cost experience in New York, with the same verbal threshold as New Jersey has been declining and is currently around 2% to 4%. Based on the available data and judgment a 10% severity trend amount was selected.

For BI frequency, there were no valid New Jersey data because of the many changes in the threshold. Therefore, although there is not necessarily a one-to-one correlation between accident frequency and injury frequency, property damage frequencies were reviewed as a surrogate for the missing data. These data show continuing drops in accident frequency as discussed above. Based on these data, a -2.5% frequency trend was selected for BI (one-half of the selected PD frequency). Note that there may be continuing shifts in the distribution of business over time toward the verbal threshold which will tend to exert further downward pressure on frequencies (and upward pressure on severities). Note also that this selection is consistent with the frequency changes observed in New York at this point in time following introduction of the verbal threshold (about four years subsequent).

A summary of the indicated and selected frequency and severity trends is shown on Exhibit 4. The selected values result in a pure premium trend of 7.3%.

Given the number and kinds of law changes that have taken place over the last several years, the ISO trend data were not useful as support for the selected BI trend.

c. Personal Injury Protection

For severity, the data relied on included the same CPI sources as referenced for BI and the New Jersey Fast Track data. In referencing the Fast Track data, it was noted that it contains distortions due to the changes in PIP coverage over the last several years such as introduction of deductibles and a co-payment. Therefore, the CPI data were given the most consideration and a conservative 10% severity trend was selected. This was then reduced by 1% to 9% in recognition of the introduction of the medical fee schedule.

The selected frequency trend of -1% was based on the observed change in the Fast Track frequency from 1987 to 1988 (the last data available prior to the 1989 law changes) of -1.9%.

A summary of the indicated and selected frequency and severity trends is shown on Exhibit 4. The selected values produce a pure premium trend of 7.9%.

Given the number and kinds of law changes that have taken place over the last several years, the ISO trend data were not useful as support for the selected PIP trend.

d. Comprehensive

Indicated trends based on New Jersey Fast Track data suffer from distortion due to shifts in distribution of business by deductible. However, current values show declining trends similar to those observed for PD. Although not directly comparable, a similar downward pattern appears in the countrywide Fast Track data.

Given that no valid data for this coverage were available, a 6% change in pure premium was judgmentally selected. This is consistent with the last available ISO trend calculated excluding wind and water losses at 8% and the currently observed CPI changes for vehicle repair costs at an average of 1.2%.

e. Collision

Because these data were also distorted due to shifts in distribution of business to higher deductibles, the same CPI sources referenced for PD were used here to select the pure premium trend of 1.7%, the same as the PD pure premium trend. A summary of the indicated and selected frequency and severity trends is shown on Exhibit 4.

f. Trend Period and Method of Application

The selected frequencies and severities were trended exponentially. The trend period was from the average date of loss in the historical experience period to the average date of loss in the ensuing experience period.

C. Expenses

1. Claim Service Fees Paid

Claim service related costs include the servicing carrier fees, directly reimbursable expenses, SIU allowance, and ale paid with MTF funds. Servicing carrier fees were treated as unallocated loss adjustment expenses (ule) and subjected to the expense trend procedure. The remaining expenses were treated as ale and included with losses.

The fixed monthly fee paid to Computer Sciences Corporation was allocated to coverage in proportion to the other expenses by coverage.

2. Non-Claim Service Fees and Other Expenses

Non-claim service fees were allocated to coverage in proportion to written premium by coverage. A 1% loading, based on observed actual costs to date, was included to cover MTF administrative costs.

3. Expense Trend

MTF costs consist primarily of fees paid to the servicing carriers for policy and claims processing. These fees are based on numbers of policies and numbers of claims. Thus, the prospective expense amounts would appropriately be derived based on projection of these underlying elements. The servicing carrier contracts also provide for CPI adjustments to the per unit costs. Due to time constraints a method of trending expenses was applied in lieu of projecting the underlying parameters. This method consists of developing a current cost factor utilizing the latest CPI indices and trending from that point to the appropriate date in the prospective experience period. For non-claim expenses this is six months beyond the expected effective date of the new rates and for claim expenses it is the expected date of loss in the prospective rating period.

The resultant current cost factor and expense trend values were 1.013 and +3.5%, respectively.

4. Other Expenses

Other expenses include commissions, premium tax, UCJF assessment, start-up costs, administrative costs of operation, and various miscellaneous expenses. The following assumptions were made regarding each expense item.

a. Commissions

These were set at the ratio of actual commissions written to premiums written as provided on the AIPSO reports. This resulted in the unexpected amounts of 8.2% for liability and 9.3% for physical damage.

b. Premium Tax

This was derived from the figures included in the MTF financial statements at 0.25%.

c. UCJF

The MTF has set aside provision for a 7.3% UCJF assessment.

d. Start-Up Costs

MTF servicing carriers were reimbursed for start-up costs in the amount of \$5.6 million. Because this was a one time cost, it was not included in the calculated required rate level indication. However, it is an amount which the MTF must fund in its rates at some point.

e. Administrative Costs

According to its financial statement, the MTF has current operating costs of about 0.7%. This was increased to 1% based on information from MTF management.

f. Miscellaneous Expenses

The MTF financial statement displayed various miscellaneous expenses which are not all captured within the MTF administrative allowance. These include items such as premiums charged off. There are also offsetting items such as commissions charged off. For expediency these items were not explicitly relected in these calculations. Their effect on the overall result would be minimal.

D. Cash Flow Analysis

The various income and outgo items were included at the values cited above. The timing of each item is described below. As noted earlier, a 5% discount factor was applied.

1. Premium Collection

The quarterly payout pattern of 58%, 14%, 28%, and 28% was based on the MTF six pay plan.

2. Loss and ALE

Absent an IBNR study, the quarterly payout pattern was taken from the Mercer July 12, 1991 draft financial report. These patterns reflect expected closure of all claims within a seven year period. These time frames appear to be too short for the liability coverages. However, no

adjustment was made. Nor were these patterns adjusted for the different IBNR estimates.

[Exhibits Omitted]

APPENDIX 15

SUBCHAPTER 29. ORDERLY WITHDRAWAL OF
INSURANCE BUSINESS

11:2-29.1 Purpose and scope

(a) The purpose of this subchapter is to establish the requirements and procedures by which insurers may undertake an orderly withdrawal from the business of insurance in this State, thereby minimizing the adverse effects upon policyholders of eliminating coverage; preventing or minimizing the disruption in the marketplace and harm to the public that would otherwise occur in the absence of regulation; and permitting insurers to wind down their business in an orderly fashion as is consistent with N.J.S.A. 17:17-10 and 17:33B-30.

(b) This subchapter applies to all insurers that seek to withdraw from the business of insurance as defined herein.

11:2-29.2 Definitions

The following words and terms, when used in this subchapter, shall have the following meanings, unless the context clearly indicates otherwise:

"Affiliate" means an insurer that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the insurer that initiates a withdrawal, as defined in N.J.S.A. 17:27A-1.

"Annual statement" means the form of statement that is described in N.J.S.A. 17:23-1.

"Applicant" means the insurer seeking approval to withdraw from the business of insurance in this State.

"Assumption agreement" means a contract between insurers whereby one insurer transfers all or substantially all its rights, duties and obligations arising from certain policies to another insurer.

"Authority" means the power granted by the Commissioner which enables an insurer to transact the business of insurance.

"Automobile" and "automobile insurance" are as defined in N.J.S.A. 17:30E-3.

"Business of insurance" or "insurance" means any kind, line, subline, or a portion thereof authorized by Chapters 17 or 32 of Title 17 of the Revised Statutes.

"Commencement date" of withdrawal means the date which the applicant may begin withdrawing from this State pursuant to the approved plan of orderly withdrawal.

"Commissioner" means the Commissioner of the New Jersey Department of Insurance.

"Control" is as defined in N.J.S.A. 17:27A-1.

"Department" means the New Jersey Department of Insurance.

"Effective date" of withdrawal means the date at which the applicant has complied with any and all conditions contained in the approved plan of orderly withdrawal.

"Insurance holding company system" consists of two or more affiliated persons, one or more of which is an insurer as defined in N.J.S.A. 17:27A-1.

"Insurance producer" or "producer" means any person engaged in the business of an insurance agent, broker or consultant, as those terms are defined in N.J.S.A. 17:22A-2.

"Insurer" means an insurer or eligible surplus lines insurer, and any insurance affiliates thereof, authorized or admitted pursuant to Chapters 17 or 32 of Title 17 of the Revised Statutes to transact in this State the business of insurance as defined herein.

"Plan" means a plan of orderly withdrawal from insurance business in New Jersey.

"Multi-state account" means a single contract or policy of commercial lines insurance as defined in N.J.S.A. 17:29AA-3 which covers risks or locations in both New Jersey and at least one other state; any group policy in which covered members of the group reside in New Jersey and at least one other state; and any plan approved for the mass marketing of insurance pursuant to N.J.A.C. 11:2-12 in which policyholders of the plan reside in New Jersey and at least one other state.

"Portfolio reinsurance agreement" means a contract between insurers whereby one insurer transfers its entire liability for in-force policies or outstanding losses, or both, to another insurer regarding a described segment of insurance business.

"Rating system" means every schedule, class, classification, rule, guide, standard, manual, table or rating plan by whatever name described containing the rates, rules and forms used by any insurer or by any rating organization in determining or ascertaining a rate.

"Reinsurance agreement" means a contract between insurers whereby one insurer agrees to insure part or all of an insurance risk of an originating, or ceding, insurer.

"Residual market mechanism" means any program authorized or created by the New Jersey State Legislature which is designed to provide an insurance market for insureds who are unable to obtain insurance in the voluntary market.

"State" means the State of New Jersey.

"Withdraw" or "withdrawal" means the nonrenewal, cancellation, or termination of policies, or surrender of authority to transact the business of insurance in this State, or any insurer action that is equivalent to a withdrawal from the business of insurance in this State which may include, but is not limited to, the elimination of a rating system, termination of agency contracts, reduction in agency commissions, restrictions on agency solicitation or binding authority, insurer refusal of applications or declaration of a dividend to an affiliate, when such action or actions exceed those occurring in the ordinary course of business. Whether the above activities are equivalent to a withdrawal shall be determined by the Commissioner on a case-by-case basis.

...

"Withdraw" or "withdrawal" also means the transfer to another insurer of insurance business pursuant to an assumption agreement as defined herein or a portfolio reinsurance agreement as defined herein.

11:2-29.3 General provisions

(a) Any insurer that seeks to undertake any of the actions described as withdrawals in N.J.A.C. 11:2-29.2 shall provide the Commissioner with written notification so that he or she may determine whether the insurer must file a plan of orderly withdrawal pursuant to N.J.A.C. 11:2-29.4 or, if such plan is waived by the Commissioner under circumstances he or she considers appropriate, a reasonable substitute withdrawal procedure approved by the Commissioner.

(b) Any insurer that is required by the Commissioner to file a plan of orderly withdrawal pursuant to N.J.A.C. 11:2-29.4 shall submit to the Department an original and five copies of a proposed plan for prior approval thereof.

1. The Commissioner shall not begin his or her evaluation of the proposed plan until the applicant has complied with the requirements contained herein for its submission. Including the submission of any additional information specifically required pursuant to N.J.A.C. 11:2-29.4(b), after which the Commissioner shall approve the plan within 120 days, subject to the terms and conditions which he or she may consider appropriate.

i. The Commissioner shall acknowledge to the applicant the receipt of any filing and request any additional information required for review pursuant to N.J.A.C. 11:2-29.4(b) within 30 days thereafter, the failure of which shall allow the applicant to treat the filing as complete.

ii. The Commissioner may extend the 120 day time frame for approval of the plan an additional 40 days for good cause and shall provide notice to the applicant of such extension.

2. An applicant shall not commence any action in furtherance of a withdrawal as defined herein prior to the Commissioner's approval thereof. For the purposes of this paragraph, commencing an action in furtherance of a withdrawal does not include the non-binding oral or written communication between an insurer/applicant and another insurer in negotiating a replacement of the insurer/applicant's insurance business by the other insurer, the negotiation of an agreement with a replacement carrier subject to approval of the Commissioner and conditioned on approval of the plan, or non-binding oral or written communications with any of the entities set forth at N.J.A.C. 11:2-29.4(a)11.

3. The authority of an applicant to conduct the business of insurance from which it seeks to withdraw, as well as any other authority which it is required to surrender pursuant to this subchapter shall, upon approval of the plan, continue in effect, but only in accordance with the plan as approved.

4. No withdrawal shall become effective until the applicant has complied with any and all conditions contained in the approved plan which relate to the effective date of withdrawal.

5. Unless the applicant specifically requests and is granted a waiver, the applicant shall make either or both of the following special deposits, as a condition of approval of the plan, in securities or the equivalent thereof in performance bonds as determined by the Commissioner, until such time as the applicant's liabilities as determined by the Commissioner no longer exist in this State:

i. A deposit established with and in the name of the Commissioner for the benefit of all of the applicant's New Jersey policyholders, claimants and creditors which shall be equal to an amount not to exceed 125 percent of the applicant's current and potential liabilities existing or that may exist in this State;

ii. A deposit established with and in the name of the Commissioner pursuant to a consent order signed by the applicant to guarantee compliance with the approved plan, a material breach of which may, upon notice to the insurer, result in an immediate forfeiture of the deposit in whole or in part. This deposit shall be in an amount established at the discretion of the Commissioner and may equal the greater of one million dollars or 10 percent of the applicant's average annual net direct premiums written within the last three years in the line(s) from which it seeks to withdraw.

6. The applicant may substitute, with the approval of the Commissioner, in place of the deposits required in (b)5i above, the following:

- i. A proper guarantee from its immediate or ultimate parent;
- ii. A letter of credit;
- iii. A trust agreement; or
- iv. Any other financial guarantee of the applicant's total liabilities.

7. For good cause shown, the Commissioner may waive the special deposits or substitutes required in (b)5 and 6 above upon a consideration of factors including, but not limited to, the uniqueness of the applicant's circumstances, its size, and its volume of business and whether the withdrawal is being effected pursuant to an assumption or portfolio reinsurance agreement.

(c) The Commissioner may require as a condition of approval of the plan the surrender of some or all certificates of authority, issued pursuant to Chapters 17 or 32 of Title 17 of the Revised Statutes, held by the applicant or by other companies within the same insurance holding company system as the applicant for amendment, termination, suspension, restriction or such other modification as the Commissioner considers appropriate. Upon specific request by the applicant for a waiver of any portion of these requirements the Commissioner may grant the waiver in whole or in part if the Commissioner finds that, based upon proofs presented, one or more of the following mitigating circumstances exist:

1. The withdrawal will not cause a market availability problem or an undue disruption in the marketplace;
2. The applicant will enter into an agreement with a proposed replacement carrier to assume the applicant's existing book of business conditioned, however, upon an approved plan;
3. The withdrawal will not adversely affect competition;
4. The withdrawal is due to specified problems affecting the solvency of the applicant;
5. The withdrawal is consistent with the insurer's overall plan of withdrawal in other jurisdictions as part of a corporate restructuring; or
6. The public interest is best served by such a waiver.

(d) If more than one insurer within the same holding company system seeks or is required by the Commissioner pursuant to this subchapter to withdraw from the business of insurance in this State, each withdrawing affiliate shall submit a separate plan to the Commissioner pursuant to this subchapter or, if such plan is waived pursuant to (a) above, a reasonable substitute withdrawal procedure approved by the Commissioner.

(e) An insurer that currently services a residual market mechanism and is subject to the withdrawal provisions contained in the plan of operation governing such mechanism is exempted from the requirements of this subchapter to the extent of the insurance business serviced by the insurer in such mechanism.

(f) The applicant and its affiliates shall be prohibited for a period of up to five years after the effective date of withdrawal from acquiring, directly or indirectly, a controlling interest in any insurer that is licensed to do business in this State without approval of the Commissioner.

11:2-29.4 Elements of proposed plan of orderly withdrawal

(a) A proposed plan of orderly withdrawal shall contain the following information supported by adequate proof of the validity thereof, if not specifically required herein:

1. The reasons the applicant seeks to withdraw, supported by a description and documentation of the applicant's financial condition for the last three years or such other period as the Commissioner considers appropriate, including the underlying accounting, actuarial and other relevant data or material relied upon in deciding to seek withdrawal;

2. The proposed commencement date of such withdrawal;

3. A description of the following:

- i. All authority currently and previously held by the applicant in all jurisdictions (specifically listing states in which the applicant has withdrawn);

- ii. The authority in New Jersey currently and previously held by its insurer affiliates, including dates of issuance, surrender, suspension or revocation; and

iii. The authority in other jurisdictions held by the applicant or its insurer affiliates that has recently been surrendered or is intended for surrender currently and in the future;

4. An organizational chart and narrative description of the relationships among the applicant and its insurer affiliates, if any, indicating at a minimum:

i. The business of insurance which each has authority to write in New Jersey;

ii. The management relationships;

iii. The financial relationships (for example, reinsurance agreements, pooling arrangements, common investments, etc.);

iv. The marketing relationships;

v. The agency relationships;

vi. The claims handling relationships; and

vii. Whether any of the applicant's insurer affiliates are also taking action or applying to withdraw from the business of insurance in this State (and if so, the details thereof);

5. A description, by line of insurance written in New Jersey, of the applicant's and its insurer affiliates' business (both property/casualty and life/health) during the last three years, including for each year the corresponding premium volume, number of current policyholders, number of exposures, approximate market share and the number of insurance producers and employees servicing the business. If employees of the

applicant or any of its affiliates will be terminated in this State as a result of the applicant's withdrawal, a description of the method of termination, a description of the termination benefits, and any other financial or nonfinancial accommodations made on the employees' behalf shall be included;

6. The address of each of the applicant's offices in this State;

7. Copies of the proposed cancellation and non-renewal notices, and termination notices, the applicant intends to send to its policyholders and insurance producers, respectively, as well as any other withdrawal-related correspondence, including the proposed dates of such notices or correspondence. Producer termination notices shall comply with the requirements contained in N.J.S.A. 17:22-6.14a;

8. In the case of a proposed withdrawal of life, health or annuity business to be effected through one or more assumption agreements, the proposed certificate(s) of assumption and letters of notification (where appropriate) to policyholders informing them of the transfer of their policies to another insurer. In the case of a proposed withdrawal of other than life, health or annuity business to be effected through one or more portfolio reinsurance agreements, the reinsurance agreement(s) and letters of notification (where appropriate) to policyholders informing them of the reinsurance of their risks with another insurer;

9. The name and address of each insurance producer, as well as the number of policies sold and premium volume produced by each producer, by line of

insurance, for a 12 month period prior to the filing of the proposed plan;

10. A specimen copy of each current producer contract;

11. Copies of all correspondence and notices to be sent to the following entities or their statutory successors, as well as a description of all agreements (which need not be in final form) reached with such entities or their statutory successors as to the applicant's financial and reporting obligations to them, as applicable; if not applicable, an explanation why. The following list is not intended to be exhaustive. It is the responsibility of the applicant to furnish the information required under this paragraph for any other statutorily created or authorized entity to which it owes or may owe a financial or reporting obligation. The Commissioner may require the applicant to deposit with any of the below-listed entities (or their statutory successors) an amount sufficient to meet the applicant's obligations thereto.

i. The Unsatisfied Claim and Judgment Fund established pursuant to N.J.S.A. 39:6-61 et seq.;

ii. The New Jersey Property-Liability Insurance Guaranty Association established pursuant to N.J.S.A. 17:30A-1 et seq.;

iii. The New Jersey Automobile Insurance Risk Exchange established pursuant to N.J.S.A. 39:6A-21 through 22.1;

iv. The Mutual Workers Compensation Security Fund established pursuant to N.J.S.A. 34:15-112;

v. The Stock Workers Compensation Security Fund established pursuant to N.J.S.A. 34:15-105;

vi. The New Jersey Insurance Division of Fraud Prevention established pursuant to N.J.S.A. 17:33A-1 et seq.;

vii. The Commercial Automobile Insurance Procedure established pursuant to N.J.S.A. 17:29D-1;

viii. The New Jersey State Division of Taxation for premium taxes required by N.J.S.A. 54:18A-1 et seq. and 17:33B-49;

ix. The Surplus Lines Guaranty Association established pursuant to N.J.S.A. 17:22-6.70 et seq.;

x. The Medical Malpractice Reinsurance Association established pursuant to N.J.S.A. 17:30D-1 et seq.;

xi. The Market Transition Facility established pursuant to N.J.S.A. 17:33B-11;

xii. The New Jersey Automobile Full Insurance Underwriting Association for examination assessments provided by N.J.S.A. 17:30E-18.1;

xiii. The New Jersey Automobile Full Insurance Underwriting Association for residual market equalization charges and policy constants established pursuant to N.J.S.A. 17:30E-8 and 17:29A-37.1, respectively; and

xiv. The Department of Insurance for examination fees provided for by N.J.S.A. 17:23-1 et seq. and other statutory fees provided for by N.J.S.A. 17:33-1;

12. A statement, by line of insurance written in this State, of all of the applicant's current incurred liabilities

and reserves, including those incurred but not reported, as developed and certified by a "qualified actuary" as defined in N.J.A.C. 11:1-21.1 for property and casualty lines and by a Fellow of the Society of Actuaries for life and health lines, as of a date not earlier than 90 days prior to the submission of the proposed plan and which shall include the following in the case of insurance other than life:

i. Copies of all work papers of the actuary supporting the actuarial opinions;

ii. Copies of all underlying statistics used by the actuary;

iii. If not included in (b)12ii above, development triangles, New Jersey only and countrywide for the following. Triangles shall be constructed as of December 31 for as many accident years and as many development years as necessary to display at least five mature accident years. For the purpose of this requirement, a mature accident year is defined as one for which paid losses equal at least 99 percent of incurred losses including IBNR. Such data shall be supplied both in hard copy and as their ASCII equivalent. Any narrative necessary for proper interpretation of the data supplied shall be provided.

(1) Paid losses;

(2) Incurred losses; and

(3) Claim counts;

(A) Reported; and

(B) Closed; and

iv. If the insurer does not have five mature accident years as required in (b)12iii above, then it shall display five accident years which are the closest to being mature, and if the insurer does not have five accident years of data, then it shall display the accident years it has.

13. A description of the manner in which the applicant has in the past three years handled and intends to handle claims, premium factor charges, premium billing, and policyholder service regarding policies held by New Jersey residents remaining in force after the plan has been approved. Provide a description of the applicant's staff and adjusters servicing these claims, including the servicing location and the procedures for consumer contact;

14. A list of all the applicant's and its affiliates' deposits, if any, currently held pursuant to N.J.S.A. 17:20-1 et seq.;

15. A description of the kind and amount of all reinsurance assumed and ceded by the applicant identifying each ceding and assuming insurer and describing the corresponding risks in each reinsurance agreement. An explanation of whether the proposed withdrawal will affect the surplus of another insurer as a result of the loss of credit received by that insurer on any of the applicant's assumed reinsurance, as well as a description of the procedures designed to minimize any marketplace disruption or hazardous financial condition that may occur as a result of the loss of credit, shall be included;

16. A description of all multi-state accounts under which insurance has been provided for risks located in

New Jersey, as well as an explanation of the impact of withdrawal on such risks;

17. The proposed amount of the special deposits required under N.J.A.C. 11:2-29.3 (b)5, which shall be maintained until such time as the applicant's liabilities and potential liabilities no longer exist in this State;

18. Written certification from a duly authorized officer of the applicant, signed under the pains and penalties of perjury, that the information submitted in the proposed plan is accurate and complete to the best of his or her belief and that for as long as insurance policies are in force or there are unpaid losses or expenses in this State:

i. The applicant shall fully honor all of its legal obligations in this State;

ii. The applicant shall continue to service, without discrimination, all outstanding policies, bonds and surety obligations, which includes processing all usual and customary endorsements requested by insureds during the term of such policies, subject to the applicant's normal underwriting standards;

iii. The applicant shall continue to submit annual statements and information required by the entities set forth in (a)11 above, upon request, for as long as the applicant has any unearned premium or any unpaid or incurred losses in this State;

iv. The applicant shall continue to operate in accordance with the laws and regulations of this State and remain subject to examination by the Department for as long as considered necessary by the Commissioner;

v. The applicant shall not accept any new business whatsoever in this State unless authorized or required by the Commissioner, including reinsurance and excess or surplus lines placements; and

vi. The applicant shall maintain its designation of the Commissioner as its agent for service of process; and

19. The plan shall include a method acceptable to the Commissioner to verify the applicant's compliance with its obligations under the plan as approved which may include, but is not limited to, quarterly financial and informational reports of the applicant's progress under the plan.

(b) The Commissioner may require any other information he or she considers relevant to the evaluation of the request to withdraw.

11:2-29.5 Replacement; non-renewal

(a) Notwithstanding the provisions of N.J.A.C. 11:3-8.3, if an applicant's request to withdraw involves private passenger automobile insurance and the applicant is required to submit a proposed plan, the applicant is subject to the following additional conditions which must be addressed in the proposed plan;

1. The applicant shall seek to place its business with a voluntary market replacement carrier or carriers acceptable to the Commissioner for a specified period of years after the Commissioner's approval of the plan or until all automobile insurance is replaced, whichever is sooner.

i. The period of time in which an applicant must seek to place its business with a replacement carrier will

be determined by the Commissioner, but in no instance will it be less than one year or more than five years. If, at the end of the designated period, the applicant has not succeeded in placing all of its private passenger automobile insurance policies with a vountary [sic] market carrier, the applicant shall begin an orderly process of nonrenewal at a rate designated by the Commissioner. In accordance with such process, the applicant shall provide two notices of nonrenewal to remaining policyholders. Unless the Commissioner finds that good cause exists for shortening the initial notice period, the first nonrenewal notice shall be provided at least one year prior to the next policy expiration date and its contents shall comply with the provisions of N.J.A.C. 11:3-8.3. The insurer shall issue a second notice of nonrenewal in compliance with the time and content requirements of N.J.A.C. 11:3-8.3.

ii. An insurer which acts as a replacement carrier for the private passenger automobile insurance business from which the applicant seeks to withdraw assumes all of the legal rights, duties and obligations associated with the participation of private passenger automobile insurers in the automobile insurance market in this State.

2. An applicant shall be required to accept the quotas established by N.J.S.A. 17:33B-11(c)5 unless the applicant specifically requests and the Commissioner agrees to a waiver of this requirement.

(b) If an applicant's request to withdraw involves other than private passenger automobile insurance, the applicant may be subject to conditions addressed either in the approved plan or, if the plan is waived pursuant to

N.J.A.C. 11:2-29.3(a), in a reasonable substitute withdrawal procedure approved by the Commissioner.

11:2-29.6 Confidentiality of plan of orderly withdrawal

(a) All data or information contained in the plan is confidential and will not be disclosed by the Department to any person other than its employees and representatives, except the following items, but only upon written, specified request and upon notice to the insurer/applicant:

1. N.J.A.C. 11:2-29.4(a)3i – Description of current and prior authority to do business by jurisdiction;
2. N.J.A.C. 11:2-29.4(a)4 – Organizational chart;
3. N.J.A.C. 11:2-29.4(a)4i – Lines of insurance written by each affiliate;
4. N.J.A.C. 11:2-29.4(a)4v – Agency relationships of affiliates by agent name, to the extent available through the Department's licensing system;
5. N.J.A.C. 11:2-29.4(a)5 – Premium volume, number of current policyholders, market share and number of producers by line of business;
6. N.J.A.C. 11:2-29.4(a)6 – Address of applicant's offices in this State;
7. N.J.A.C. 11:2-29.4(a)7 – Policyholder nonrenewal and producer termination notices;
8. N.J.A.C. 11:2-29.4(a)9 – Name and address of each insurance producer to the extent available through the Department's licensing system;

9. N.J.A.C. 11:2-29.4(a)11 – Copies of all correspondence and notices sent to various entities, as approved, to which the applicant owes a financial obligation;

10. N.J.A.C. 11:2-29.4(a)12 – Certified statement of New Jersey incurred liabilities and reserves;

11. N.J.A.C. 11:2-29.4(a)14 – Deposits held by a custodian on behalf of the Commissioner; and

12. N.J.A.C. 11:2-29.4(a)17 – Establishment of special deposits or equivalent performance bonds as approved.

11:2-29.7 Fines and penalties

Failure to comply with this subchapter may result in the imposition of sanctions by the Department including, but not limited to, sanctions pursuant to N.J.S.A. 17:33-2.

11:2-29.8 Severability

If any provision of this subchapter or its application to any person or circumstance is held invalid, such determination shall not affect other provisions or applications of this subchapter which can be given effect without the invalid provision or application, and to that end the provisions of this subchapter are separable.

APPENDIX 16

ORDER NO.: A91-279

STATE OF NEW JERSEY
DEPARTMENT OF INSURANCE

IN THE MATTER OF:	)	ADMINISTRATIVE
ALLSTATE INSURANCE	)	ACTION
COMPANY PRIVATE	)	Agency Docket Nos.:
PASSENGER	)	90-1044 & 90-1320
AUTOMOBILE RATE	)	OAL Docket No.:
FILING	)	INS-565-915
(APPLICATION FOR	)	DECISION AND ORDER
INTERIM RATE)	
RELIEF))	

This matter comes before the New Jersey Commissioner of Insurance (Commissioner) pursuant to the provisions of *N.J.S.A. 17:29A-1 et seq.*, *N.J.S.A. 17:1C-6* and *N.J.S.A. 52:14B-1 et seq.* and all powers expressed or implied therein.

Procedural History

On August 24, 1990, Allstate Insurance Company (Allstate) filed for approval of a private passenger automobile rate change seeking an overall statewide rate level increase of 8.6 percent. This proposed increase seeks to include in the base premiums the surtax and assessments incurred under the Fair Automobile Insurance Reform Act of 1990, P.L. 1990, c.8 (FAIR Act). In its transmittal letter, Allstate requested that if the rates were not approved within 30 days, then the Commissioner should

convene a hearing to consider the merits of the application. By letter dated September 28, 1990 Allstate reiterated its request for a hearing. After further correspondence between Allstate and the Department of Insurance (Department) concerning the completeness of the filing, Allstate commenced an action in the Superior Court, Chancery Division, which resulted in an Order dated December 20, 1990 which found the filing to be complete and directed that the matter be transferred to the Office of Administrative Law (OAL) for hearing. The matter was so transmitted on January 4, 1991.

On October 16, 1990 Allstate filed for approval of a private passenger automobile rate change seeking an overall statewide rate level increase of 27.7 percent independent of the surtaxes and assessments imposed by the FAIR Act. Allstate again requested a hearing on the filing if the rate increase was not approved within 30 days. This second matter was transferred to the OAL for hearing on November 30, 1990.

The Division of Rate Counsel, Office of the Public Advocate (Public Advocate) has intervened in both matters. Hearings before the assigned Administrative Law Judge (ALJ) commenced February 6, 1991 and have continued to date.

On January 17, 1991 Allstate filed separate applications in both of these proceedings seeking emergent, interim rate relief. Department staff and the Public Advocate filed letter briefs opposing the applications on January 28 and January 24, respectively.

Contentions of the Parties

Allstate requests that it be permitted to implement its proposed rate increases, as filed, on an interim basis pending final decision upon completion of the hearings. The increase would be refunded should Allstate not prevail. Allstate asserts that payment of the FAIR Act surtaxes and assessments caused it to lose \$26.4 million in 1990 and that its losses are continuing at the rate of over \$69,000 each day. Since new rates fixed as a result of the pending proceedings may only be applied prospectively, these current losses will never be recoverable. Allstate thus asserts that it is sustaining irreparable harm which entitles it to interim rate relief pursuant to the Uniform Rules of Administrative Procedure, *N.J.A.C. 1:1-12.2*. Allstate asserts that the Commissioner's general statutory powers under *N.J.S.A. 17:1-1* and *17:1-2* (see also *N.J.S.A. 17:1C-6*) authorize him to approve interim rates on an emergency basis, which authority has been recognized in appropriate circumstances. *N.J. State AFL-CIO v. Bryant*, 55 171 (1969); *N.J. Land Title Insurance Rating Bureau v. Sheeran*, 151 *N.J. Super.* 45 (App. Div. 1977).

In opposition to Allstate's interim rate application, the Department's staff contends that the Legislature, in *N.J.S.A. 17:29A-14e*, has delineated the limited circumstances in which the Commissioner may grant rate relief and by such delineation has implicitly prohibited any other use of interim rates. Department staff argues that *N.J.S.A. 17:29A-14e* sets forth certain circumstances in which the Commissioner may set interim rates prior to a hearing and that such delineation must be read as evidence that the Legislature did not intend for interim rates

to be set in other circumstances. In support of this argument staff cites a general principal of statutory construction which holds that where a manner of performance is statutorily designated there is an inference that all omissions are exclusions. 2A Sutherland *Statutory Construction* Section 47.23: *Shapiro v. Essex County Freeholder Board* 177 N.J. Super. 87 (Law Div. 1980) Staff also notes that in *N.J. State AFL-CIO v. Bryant*, 55 N.J. 171 (1969), which was cited by Allstate as support for the Commissioner's implied authority to set interim rates, no statutory mandate for a prior rate hearing existed; whereas here a prior hearing is required pursuant to N.J.S.A. 17:29A-14. Alternatively, Department staff asserts that even if interim ratemaking authority does exist, Allstate has failed to meet its burden of justifying rate relief prior to the conclusion of the pending permanent rate cases.

The Division of Rate Counsel, Department of the Public Advocate (Public Advocate), similarly opposes Allstate's interim applications on the ground that the Commissioner lacks authority to grant them and, alternatively, that Allstate has failed to show its entitlement to such relief. The Public Advocate contends that the cases relied upon by Allstate do not support its application, and that approval of interim rates would subvert the regulatory scheme.

Decision

N.J.S.A. 17:29A-14 addresses the alteration of rates by personal lines of property and casualty insurers. Paragraph a of that statute provides that insurers may alter or amend their rates and rating systems only with the prior

approval of the Commissioner. Paragraph c then provides as follows:

c. If an insurer or rating organization files a proposed alteration, supplement or amendment to its rating system, or any part thereof, which would result in a change in rates, the commissioner may, or upon the request of the filer or the Public Advocate shall, certify the matter for a hearing. The hearing shall, at the commissioner's discretion, be conducted by himself, by a person appointed by the commissioner . . . or by the Office of Administrative Law . . . as a contested case. . . .

Thus the Legislature has provided that rate changes such as those proposed by Allstate may not be implemented without prior approval of the Commissioner after an opportunity for a hearing, if requested by the filer or the Public Advocate, or otherwise determined to be necessary by the Commissioner in the absence of a request from either. In both present matters Allstate itself requested hearings.

Allstate's applications squarely present the question whether the Commissioner has authority to approve an interim rate increase for a personal lines property-casualty insurer when a hearing on the proposed rate change has been requested and is pending. For the reasons set forth below, I find that the Commissioner does not have such authority, and am therefore constrained to dismiss both applications. I further find that even if such authority did exist, however, I would not choose to exercise it for reasons set forth below.

Allstate asserts that it is entitled to an interim rate increase because it is suffering irreparable harm, citing N.J.A.C. 1:1-12.6(a). While that rule provides jurisdiction to grant emergency relief "{w}here authorized by law and where irreparable harm will result . . . ", reliance upon it to provide independent authority in the Commissioner to approve a rate change prior to the conclusion of a requested hearing is misplaced, since it merely begs the question whether such an action is authorized by law.

In other contexts the general powers of the Commissioner under N.J.S.A. 17:1-1 et seq. have been found in two cases to include the authority to approve rates on an interim basis. Nevertheless, as the discussion below concludes, neither of those cases provides support for authority to act in the present matter.

In *N.J. State AFL-CIO v. Bryant*, 55 N.J. 171 (1969), the Supreme Court affirmed the Commissioner's decision to approve increased rates for an applicant that was in serious financial distress pending a final determination on its application for permanent new rates. In a hearing commenced but not concluded, evidence showed that the applicant, Blue Cross, had a substantial and growing deficit; was technically insolvent; and was operating without required minimum reserves. 55 N.J. at 174. The parties to the hearing, including counsel appointed to represent the public interest, acknowledged that an immediate rate increase was required simply to stabilize Blue Cross's deficit at the existing level pending a final decision. The rates approved were the minimum required to do so and to which all parties agreed. The Court noted that the statutes applicable to Hospital Service Corporation rate changes, N.J.S.A. 17:48-6.5 and 17:48-9, neither

required the express prior approval of rates nor mandated that a hearing be held. Under such circumstances, the Court concluded:

"There is no provision in the statute barring an interim rate increase pending completion of a hearing as to the adequacy or inadequacy of either existing or proposed rates. *In the absence of an express prohibition*, the broad language of the authority conferred on the Commissioner ought to be deemed by implication to carry power for interim relief." 55 N.J. at 176 (emphasis added).

Similarly, in *N.J. Land Title Insurance Rating Bureau v. Sheeran*, 151 N.J. Super. 45 (Law Div. 1977), the Commissioner was required to approve new, initial rates for title insurance under a newly enacted regulatory scheme. As of the statutory deadline for approval of the new rates, the hearing had not concluded. Failure to approve rates for title insurance would have seriously disrupted the market for the transfer of real estate. All parties at the hearing agreed that a rate must be established; the applicant asserted that the temporary rates should be those higher rates set forth in its filing, while the Public Advocate argued that the pre-existing, lower rates should continue to be used. The Commissioner directed continued use of the pre-existing rates during the hearing process. In upholding this exercise of authority by the Commissioner, the court stated:

"We, moreover, regard it as both essential and well settled that the scope of the Commissioner's broad administrative powers conferred by N.J.S.A. 17:1-1, 2 must be construed to

include interim rate making *not expressly proscribed by the statute*. *N.J. State AFL-CIO v. Bryant*, 55 N.J. 171, 176 (1969)." 151 N.J. Super. at 53 (emphasis added).

The Court then found that no express provision of the Title Insurance Law prohibited the action challenged, which was determined to be an emergent and transitional fixing of rates, not rate structuring under the Act.

The emphasized language in both of the cases set forth above indicates to me that the Commissioner's implied or general power to fix interim rates cannot supersede express direction from the Legislature to approve a rate change only after hearing, if one is requested. *N.J.S.A. 17:29A-14c* specifically provides that: "The Commissioner . . . upon the request of the filer or the Public Advocate, *shall* certify the matter for a hearing." (Emphasis added). I find that this specific requirement of the ratemaking statute applicable to these proceedings precludes granting the relief requested here. Although Allstate asserts that the authority to approve interim rates is not specifically prohibited, the Legislature need not both mandate that an act be done, and forbid the failure to do it, in order to convey its intent to executive officers.

This construction of the ratemaking statute is buttressed by the specific authority granted in *N.J.S.A. 17:29A-14e* to set initial rates for certain optional coverages on an interim basis, subject to hearing and subsequent adjustment. I recognize that the principal of statutory construction relied upon by staff in construing *N.J.S.A. 17:29A-17e* as an absolute prohibition against any

form of interim ratemaking has been held to be inapplicable "where there is some special reasons for mentioning one thing and none for mentioning another which is otherwise within the statute." 2A Sutherland *Statutory Construction* Section 47.23 at p. 194. In enacting N.J.S.A. 17:29A-14e, the Legislature specifically addressed the optional automobile insurance coverages, and while this provision should not be read, in itself, as a prohibition against interim ratemaking authority, I interpret it in conjunction with N.J.S.A. 17:29A-14c as expressing an assumption by the Legislature that a hearing is required when requested.

The mandate in N.J.A.C. 17:29A-14c for a contested case hearing when requested prior to changes in personal lines property-casualty insurance rates may be contrasted with the statutory scheme for adjustment of public utility rates by the Board of Public Utility Commissioners (Board). N.J.S.A. 48:2-21(b) provides that: "The board may after hearing, upon notice, by Order in writing . . . [f]ix just and reasonable individual rates, joint rates, tolls, charges or schedules. . . ." N.J.S.A. 48:2-21.1 then provides, however, that the Board may by agreement with the public utility adjust the rates during the pendency of the hearing. Thus despite the hearing requirement, the Board is specifically empowered by the Legislature to grant interim rate changes. No comparable authority is provided to the Commissioner of Insurance in matters coming before him pursuant to N.J.S.A. 17:29A-14.

Moreover, it must be noted that the Legislature has recently established an alternate remedy to an increase in rates when an insurer is faced with financial hardship as

Allstate complains of here. Sections 95 through 99 of the FAIR Act (N.J.S.A. 17:33B-52 through 17:33B-56) provide relief when an insurer's financial condition will become unsafe or unsound if the insurer is required to comply with various duties required under that Act. True hardship, which could be considered "irreparable harm", can follow if an insurer's financial condition is unsafe or unsound, because the result can be a declaration of insolvency, appointment of a receiver or a decreased rating from one of the major rating agencies, any of which is irretrievably adverse to an insurer's market reputation and thus its ability to attract both investors and insurance business. Those statutes provide that in such circumstances the insurer may apply to the Commissioner for an exemption, abatement or deferral of the surtax, assessments and other obligations. Many insurers have done so and the Commissioner has, when appropriate, granted this form of relief.

Even if the Commissioner did have the power pursuant to N.J.S.A. 17:29A-14 to approve an interim rate increase when a hearing has been requested, I find that such authority should not be used under the circumstances presented here. New Jersey's courts have long recognized that assuming the power to grant interim relief requires a most sensitive exercise of discretion. When confronted with extraordinary circumstances that may call for the exercise of that discretion, our judiciary has been guided traditionally by certain fundamental principles. Those principles are set forth in *Crowe v. DeGioia*, 90 N.J. 126, 132-34 (1982) to require the following:

(1) Irreparable harm;

(2) Uncontroverted material facts, *i.e.*, a reasonable probability that the applicant will ultimately succeed on the factual merits; and

(3) Settled law, *i.e.*, a reasonable probability that the applicant will ultimately prevail on the legal merits;

(4) A showing that the relative hardship to the applicant if relief is denied is disproportionately greater than the hardship to the applicant if the relief requested is granted. An examination of these principles in the context of the present case clearly demonstrates that interim rate relief is inappropriate in matters such as this one.

As noted in the case law applying the standard for injunctive relief, "[h]arm is generally considered irreparable in equity if it cannot be redressed adequately by monetary damages." *Crowe v. DeGioia*, 90 N.J. 126, 132-33. In ratemaking situations the New Jersey Supreme Court has recognized that some money will necessarily be irretrievably lost during the administration of the procedures required to change regulated rates. *Helmsley v. Borough of Fort Lee*, 78 N.J. 200 (1978); *In Re: New Jersey Power and Light Co.*, 15 N.J. 82 (1954). Since N.J.S.A. 17:29A-14 nevertheless requires a hearing if requested prior to an order by the Commissioner approving a rate change (except under the "flex rating" provisions; see N.J.S.A. 17:29A-44), both the Court and Legislature have determined that the loss of revenue of which Allstate complains is not "irreparable harm".

Secondly, interim relief must be based on material facts to which there is no bona fide dispute, so that the decision maker may be reasonably confident that the applicant will ultimately succeed on the factual merits. One can hardly imagine a matter in which there is more dispute concerning the material facts than the present one, which at this writing has consumed 40 days of hearings and is still continuing. While Allstate's brief recites certain facts concerning the procedural history of its filings, the facts material to a determination of this matter are those that address the substance of its rate change request.

Thirdly, interlocutory relief requires settled law, likewise to provide the decision maker with reasonable confidence that the applicant will ultimately prevail on the legal merits. The legal issues at the hearing, which include various asserted alternatives to the Department's standard ratemaking methodology set forth in *N.J.A.C. 11:3-16.10*, are likewise vigorously disputed.

Finally, a case for interim relief requires a balancing of the relative hardship to the parties. The Legislature has, I believe, struck that balance by precluding approval of a rate increase before a requested hearing is held. It is appropriate that they have done so, particularly when the subject involves a mandatory purchase of insurance. This is the case with private passenger automobile insurance which is required by statute to be maintained as a condition of owning and operating a vehicle. *N.J.S.A. 39:6A-1*. It should be noted that the statutory requirement for a hearing in automobile insurance rate increase requests was added to the ratemaking statute in 1983 (P.L. 1983, c. 65) after the decision in *N.J. State AFL-CIO v. Bryant*,

supra, and *N.J. Land Title Insurance Rating Bureau v. Sheeran, supra*, and after the creation of the Public Advocate with its duty "to represent and protect the public interest" in ratemaking. (P.L. 1974, c.27; *N.J.S.A.* 52:27E-18). The public who must purchase insurance has been provided with both a right to a hearing on changes in the rates they must pay, and the Public Advocate to represent them at the hearing. To approve an interim rate increase would serve to deprive the public of its right to a hearing by which its interests are determined, and would be inconsistent with the nature of contested case proceedings.

Furthermore, in balancing the relative hardship to the parties, I note that *N.J.S.A.* 17:29A-44 permits automobile insurers to increase their rates each year by a percentage tied to the consumer price indices. These automatic, annual increases may mitigate any financial hardship to rate increase filers during the hearing and decision procedures. * In sum, interim rate relief would never be appropriate in cases such as this one, where a private passenger automobile insurer seeks an increase in rates, and a hearing has been requested and is being vigorously controverted.

In the present matter, Allstate has asserted its entitlement to approval of an interim rate increase because of the alleged harm it is sustaining as a result of its payment of the FAIR Act surtaxes and assessments. As noted above, Allstate has an alternate remedy available in that it may apply for exemption, abatement or deferral of

* Allstate implemented a 6.46% "flex rate" increase on July 1, 1990 and has filed to implement a further 7.03% "flex rate" increase on July 1, 1991.

those obligations in accordance with *N.J.S.A. 17:33B-52 et seq.*, should it qualify to do so. Under these circumstances, the application to approve increased rates pending final determination in the proceedings now underway must be denied.

Now, therefore,

IT IS on this 28th day of June, 1991

ORDERED that the pending petitions of Allstate Insurance Company for interim rate increases be, and hereby are, dismissed.

June 28, 1991

Date

/s/ Samuel F. Fortunato

Samuel F. Fortunato
Commissioner

DB41/ORDERS

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No. 91-983

Supreme Court, U.S.

FILED

JAN 16 1992

OFFICE OF THE CLERK

In The
Supreme Court of the United States

October Term, 1991

ALLSTATE INSURANCE COMPANY,
an Illinois Corporation,

Petitioner,

v.

SAMUEL F. FORTUNATO,
Commissioner of Insurance of The State of New Jersey,

Respondent.

Petition For A Writ Of Certiorari To The
Appellate Division Of The Superior Court
Of The State Of New Jersey

RESPONDENT'S BRIEF AND APPENDIX
IN OPPOSITION TO PETITION FOR
A WRIT OF CERTIORARI

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On the Brief

COUNTERSTATEMENT OF THE QUESTION PRESENTED

May a State, consistent with the Due Process Clause of the Fourteenth Amendment, order an insurance company to take on new business at rates higher than its current voluntary market rates, where a State appellate court has found, on appeal of that order, that the company has not demonstrated that the higher State mandated rates are confiscatory such that the company would be entitled to an interim rate increase in advance of implementation of the order?

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LAWS CITED

<i>L.</i> 1988, <i>c.</i> 199, §25	3
<i>L.</i> 1990, <i>c.</i> 8	3

RULES CITED

<i>Sup.Ct.R.</i> 10.1(b)	15
<i>Sup.Ct.R.</i> 10.1(c)	8, 15



COUNTERSTATEMENT OF THE CASE

Pursuant to a legislative directive to depopulate, or downsize, the New Jersey Automobile Full Insurance Underwriting Association ("JUA") and the Market Transition Facility ("MTF") in preparation for a new automobile insurance assigned risk plan, the New Jersey Commissioner of Insurance issued orders on January 24, 1991 assigning exposures (automobiles) to insurers, including petitioner Allstate Insurance Company ("Allstate"), that had not complied with their statutory obligations to insure a certain number of risks in the voluntary market (Pet. App. 1).^{*} See N.J.S.A. 17:30E-14; 17:33B-11. Under the statutory scheme, insurers are permitted to charge these assigned insureds the higher rates applicable to persons presently insured by the MTF. The legislatively-mandated depopulation assignments are an essential part of the transition from the JUA, which had insured up to 50% of New Jersey's drivers, to the new assigned risk plan, which should provide insurance to only 10% of New Jersey's drivers. See N.J.S.A. 17:33B-11; 17:33B-12.

Petitioner Allstate, which did not write its statutorily required share of former JUA insureds and so was assigned exposures, challenged the depopulation program as unconstitutional because, Allstate averred, under no conceivable set of circumstances could it realize a just and reasonable return. Allstate's assertions are based on predictions of higher risks and inadequate rates; however, the evidence presented below did not substantiate

^{*} "Pet. App." refers to Allstate's appendix filed with the petition for a writ of certiorari.

these assumptions. The New Jersey Superior Court, Appellate Division rejected these contentions and affirmed the Commissioner's orders (Pet. App. 2). The Supreme Court of New Jersey denied Allstate's petition for certification (Pet. App. 3).

All New Jersey drivers are required to obtain automobile insurance as a condition of owning and operating an automobile. *N.J.S.A. 39:6A-1 et seq.* Between 1970 and 1983, drivers who could not obtain insurance in the voluntary market were apportioned among all insurers doing business in New Jersey, who were obligated to extend coverage pursuant to an assigned risk plan. *See N.J.S.A. 17:29D-1.* This system was changed in 1983, when the Legislature created the New Jersey Automobile Full Insurance Underwriting Association ("JUA") to provide such drivers with insurance coverage at statutorily-set rates. *See N.J.S.A. 17:30E-1 et seq.*

The JUA operated through servicing carriers which undertook the administrative responsibility of providing coverage and adjusting claims. *N.J.S.A. 17:30E-7e.* However, all claims and liabilities arising from JUA policies were paid by the JUA and not by the servicing carriers. *Ibid.* The JUA derived income from a number of sources other than premium payments, including Department of Motor Vehicle surcharges for certain violations, and charges imposed, on a per vehicle basis, on all automobile insurance policies. *N.J.S.A. 17:30E-8.* Essentially, because driving an automobile is a necessary part of life in New Jersey, automobile insurance policies for drivers who could not otherwise obtain insurance (and might then drive uninsured) were subsidized by all drivers.

However, while the JUA was in existence more and more persons were being refused coverage in the voluntary market, sometimes regardless of their driving records, and by 1988 the JUA was providing insurance to over 50% of New Jersey's drivers.* The Legislature, recognizing that the burgeoning JUA was no longer serving its purpose of providing coverage to only a limited number of drivers, passed amendments to the automobile insurance statutes to downsize, or depopulate, the JUA over a period of time. L. 1988, c. 199, §25 (amending N.J.S.A. 17:30E-14). The Legislature thus established a program to require insurers to write an increasing percentage of JUA insureds in the voluntary market pursuant to yearly quotas for the industry and apportioned shares of that quota for each insurer authorized to conduct automobile insurance business in New Jersey. *Ibid.* The amendments provided that in the event the aggregate industry depopulation quota for exposures (automobiles) to be insured in the voluntary market is not met, the Commissioner of Insurance would assign exposures from the JUA to insurers that did not meet their apportionment shares. *Ibid.*

New Jersey's automobile insurance system was again comprehensively revised on March 12, 1990 by the Fair Automobile Insurance Reform Act, L. 1990, c. 8 ("FAIR Act"). The FAIR Act eliminated the JUA, directing it not

* Under the JUA system, insurers had an incentive to write only the cleanest risks voluntarily; any applicant without a proven long-term clean record could be shifted to the JUA since then the insurer would not be liable for any claims arising under the policy.

to issue any policies after October 1, 1990, and created the Market Transition Facility ("MTF") to provide automobile insurance to JUA insureds and persons unable to obtain insurance in the voluntary market between October 1, 1990 and October 1, 1992.* After October 1, 1992, automobile insurance policies for persons unable to obtain insurance in the voluntary market will be written by insurers pursuant to an assigned risk plan. FAIR Act, §24 (N.J.S.A. 17:33B-12). The FAIR Act also accelerated the schedule for the depopulation of the JUA and MTF in preparation for the assigned risk plan. FAIR Act, §§20, 88 (N.J.S.A. 17:30E-14; 17:33B-11). Pursuant to the accelerated depopulation schedule, only 32% of exposures would be covered by the JUA or MTF by October 1, 1990; 29% by April 1, 1991; 20% by October 1, 1991 and 10% by April 1, 1992. *Ibid.* If the industry quota is not met, the statutes direct the Commissioner to assign exposures to insurers that had not met their apportionment shares. *Ibid.*

The October 1, 1990 industry quota was not met. In accordance with N.J.S.A. 17:30E-14 the Commissioner issued orders on January 24, 1991 assigning exposures to the 44 insurers that did not meet their apportionment shares, including petitioner Allstate (Pet. App. 1). Twenty-four insurers, including several large companies, had met their shares and were not assigned exposures

* The MTF, an unincorporated association of insurers authorized to conduct automobile business in New Jersey, is operated by the Commissioner of Insurance in consultation with an Advisory Board, comprised of various industry representatives. FAIR Act, §88 (N.J.S.A. 17:33B-11).

(CPa77).^{*} Attached to the orders was the Mandatory Depopulation Assignment Plan, which set forth the manner in which assignments were made. The Plan provided that JUA/MTF insureds who reside in the areas in the State that are most underrepresented in the voluntary market would be assigned first, until the percentage of JUA/MTF insureds in those areas is brought up to the level of the industry quota (*i.e.*, 32% for October 1, 1990 quota) (CPa8). The Plan further provided that the insurers offer assignees one-year policies (CPa28).

Finally, and most significantly, section 89 of the FAIR Act (N.J.S.A. 17:33B-12) permits these insurers that did not meet their apportionment shares to charge assigned insureds MTF rates, which are generally higher than the insurer's own voluntary market non-standard or standard rate.

Allstate, which did not meet its apportionment share, appealed the Commissioner's January 24, 1991 orders assigning it exposures (CPa72). The appeal was accelerated by the Appellate Division, and the depopulation program was stayed. *Ibid.* Prior to oral argument before

^{*} Ra refers to respondent's Appellate Division appendix; Rra refers to respondent's Appellate Division reply appendix; ALb refers to the brief filed by petitioner Allstate in the Supreme Court of New Jersey. Additional citations are to briefs and appendices filed by co-petitioners in the Supreme Court of New Jersey. These materials are part of the record below although the co-petitioners did not file petitions with this Court. AEb refers to petitioner Aetna's brief; AEa refers to petitioner Aetna's appendix; CPb refers to petitioner Colonial Penn's brief and CPa refers to petitioner Colonial Penn's appendix.

the Appellate Division, the Commissioner amended the Depopulation Plan so that persons with nine or more points (*i.e.*, moving vehicle violations and other infractions) would remain in the MTF; only those persons with fewer than eight points would be assigned to and covered by insurers. The amendments, transmitted to insurers after oral argument, provided that insurers screen assigned insureds and return to the MTF all assignees that are "ineligible" as defined in *N.J.A.C. 11:3-34.1 et seq.* See CPa32.

Before the Appellate Division rendered its decision, the Commissioner approved an 18.6% overall average rate increase for MTF insureds (Ra19). Thereafter, following a separate appeal by Allstate concerning the adequacy of this rate increase, the Commissioner's staff filed for an additional 15% rate increase, which the Commissioner implemented. (Pet. at 17).

On May 20, 1991 the Appellate Division affirmed the Commissioner's January 24, 1991 depopulation orders (Pet. App. 2). The Appellate Division rejected Allstate's takings arguments, holding that Allstate had not proven that MTF rates would be facially inadequate to cover the costs of insuring assigned drivers. In fact, the record before the Court contained submissions from both the Insurance Department Staff and the Public Advocate Division of Rate Counsel which indicated that Allstate's existing rates were too high and should be reduced. (R. App. 1, 2, and 3). The Appellate Division further held that the Commissioner's decisions to assign insureds from underrepresented territories first, and to require one-year policies be issued, were reasonable. Finally, the Appellate Division invalidated the part of the program

that required insurers to do business with the assigned insureds' producers.* Allstate filed a petition for certification to the Supreme Court of New Jersey, which was denied on September 18, 1991 (Pet. App. 3). Allstate's petition to this Court for a writ of certiorari followed.

SUMMARY OF ARGUMENT

Allstate's petition requests this Court to intervene in an essentially fact-based dispute over its entitlement to interim rate relief. The petition should be denied because the proceedings below are being properly handled by the Insurance Commissioner and the State's courts, in accordance with well established constitutional principles enunciated by this Court. Allstate failed, on the evidence submitted, to establish to the satisfaction of the Commissioner or the Appellate Division that the MTF rates, which are higher than Allstate's own rates, will be confiscatory. Moreover, Allstate's claim of an absolute right to protection against any possible financial loss due to rate lag is without merit. For these reasons, Allstate's facial challenge to the depopulation order at issue here was properly rejected by the State court below. Since Allstate raises no valid or significant constitutional objections to the ruling below, the petition for a writ of certiorari should be denied.

* On December 31, 1991, the Commissioner issued a revised order to Allstate which changed this aspect of the program.

ARGUMENT

THE PETITION SHOULD BE DENIED BECAUSE ALLSTATE FAILED IN THE STATE PROCEEDINGS BELOW TO PRESENT A SUFFICIENT FACTUAL BASIS FOR INTERIM RATE RELIEF AND BECAUSE ALLSTATE HAS PRESENTED NO MERITORIOUS CONSTITUTIONAL ARGUMENTS WHICH WOULD JUSTIFY REVIEW BY THIS COURT.

Upon review of its petition for a writ of certiorari, it is clear that Allstate has presented no questions which require review by this Court. It is clearly established by this Court, and well recognized in New Jersey law and New Jersey court decisions, that a rate regulated entity such as a public utility or insurance company has a constitutional right to earn a reasonable rate of return on its investments. *Duquesne Light Co. v. Barasch*, 488 U.S. 299 (1989); N.J.S.A. 17:33B-2g; *State Farm v. State of New Jersey*, 124 N.J. 32, 590 A.2d 191 (1991). This principle was recognized by the Appellate Division below. *In re Matter of Assignment of Exposures to Aetna Casualty & Surety Co., Allstate Insurance Co. and Colonial Penn Insurance Co.*, 248 N.J. Super. 367, 591 A.2d 631 (App. Div. 1991) (Pet. App. 2). This is not a case in which a state's appellate courts have adopted an erroneous rule of law which requires correction by this Court. *Sup.Ct.R.* 10.1(c). Compare *First English Evangelical Lutheran Church v. Los Angeles County*, 482 U.S. 304 (1987). Rather, this case represents a cogent, well-reasoned application by the New Jersey Superior Court, Appellate Division, of settled principles of law in a case in which there are hotly contested factual issues and in which the insurer here simply failed to establish as a matter of fact that it was entitled to interim rate relief.

Having failed to convince the State court below, on the factual record, of its right to interim relief, petitioner Allstate now nevertheless claims that it was denied an appropriate judicial process for judging its request for rate relief (Petition at 28) or, in the alternative, that the State may not impose the depopulation plan at issue here without first holding a plenary hearing on the rate impact of the plan on the subject insurance companies. Taken to its logical extension, Allstate's position is that it has an absolute constitutional right to protection against regulatory lag, and that a state therefore may not impose any regulatory requirements on insurance companies (or by implication, utilities either) without first holding a proceeding to determine the rate impact on the regulated entities and adjusting their rates prospectively to ensure their absolute protection against any financial loss resulting from the proposed new regulatory requirement. Allstate's contentions are totally lacking in merit.

In fact, as the Appellate Division's decision below clearly indicates, Allstate has already had an opportunity for judicial review of its claim for interim rate relief. Neither the Insurance Commissioner nor the Court, however, have found Allstate's factual claims persuasive enough to justify such relief.* Therefore, even by the

* It must be remembered that granting interim rate increases to insurance companies in a state such as New Jersey where all drivers are required to have insurance, places an immediate and substantial financial burden on that company's customers without giving them the benefit of a full adjudication of the merits of the company's claim for rate relief. Consequently, any claim for interim rate relief based on a company's asserted

(Continued on following page)

standards Allstate suggests in its own petition, *i.e.*, those applicable to motions for preliminary injunctive relief, (Petition at 28 n.25), it would not be constitutionally entitled to relief here.

Indeed, as the Appellate Division noted below,

The record before us is full of significant and irreconcilable factual differences. The insurers offer complex financial analyses and the assurance of their actuaries and executives that they are losing millions of dollars on their current New Jersey business. They say the near future promises even greater losses with or without their assigned JUA/MTF business, that the Commissioner is dragging his feet in considering their rate filings, and that forcing more business on them at insufficient rates is confiscatory. The Commissioner offers equally complex analyses and the assurance of his actuaries that the insurers are really doing just fine, and that their complaints are baseless. [Pet. App. 2 at 62].

The record supports this view. Ranged against Allstate's dire predictions of financial loss are expert testimony from both the Commissioner's staff and the State Public

(Continued from previous page)

right to an absolute guarantee against any possible financial loss due to regulatory lag, must be weighed against the financial burden that its request will place upon thousands of ordinary citizens who may already be struggling to pay existing rates. The fact that rates may be interim, and hence subject to eventual refund, does not necessarily mitigate the temporary financial hardship which a rate increase, which later proves to be unjustified, immediately places upon the company's insureds.

Advocate Division of Rate Counsel (R. App. 1, 2 and 3) showing that Allstate in fact is overearning and that its rates should be decreased rather than increased.*

Moreover, Allstate has chosen in its brief to this Court to bury in footnotes certain significant information which undercuts its position. Not only will Allstate be allowed to charge the new exposures the MTF rate, which is higher than Allstate's regular voluntary market rate, but that MTF rate has already been raised twice, once through an 18.6% increase in rates of poorer drivers and a second 15% increase on rates paid by better drivers. Moreover, New Jersey law allows all insurance companies the benefit of annual "flex rate" increases which may be instituted without a rate hearing. *N.J.S.A.* 17:29A-44(a), -44(f). These increases are based on a percentage of specified components of the Consumer Price Index *plus* 3%, thus cushioning the companies against losses due to regulatory lag. Allstate sheepishly admits (Petition at 29 n.26) that it has taken three of these increases since March 1989. Hence, unlike *Prendergast v. New York Telephone Co.*, 260 U.S. 43 (1923), in which there was clear proof of confiscatory rates, resulting from an order to *reduce* rates, here there is simply an order by the Insurance Commissioner to cover certain customers, as

* The Appellate Division specifically found that "the insurers do not make a case of sufficient strength to justify our entering an order freezing in place a currently disastrous insurance industry situation until the insurers' hyperbole can be tested against the Commissioner's incredulity. The resulting turmoil in the State's auto insurance industry would be intolerable." [Pet. App. 2 at 63].

clearly authorized by *California Auto Association v. Maloney*, 341 U.S. 105 (1951), and there is no proof of confiscatory rates. Moreover, the company here is permitted to charge the new customers a rate higher than its voluntary rate. Compare *Jersey Central Power & Light Co. v. F.E.R.C.*, 810 F.2d 1168 (D.C. Cir. 1987) (company ordered to reduce rates without hearing); *Smith v. Illinois Bell Co.*, 270 U.S. 587 (1926) (delay of three years in ruling on rate petition where no dispute that existing rates were confiscatory); *Banton v. Belt Line Ry. Corp.*, 268 U.S. 413 (1925) (company denied rate increase for 8 years; no dispute that rates were confiscatory). Clearly there was no due process or other constitutional violation in the Commissioner's denial of interim relief in this case.

Finally, it should be noted that in separate pending proceedings to increase Allstate's voluntary market rates, the Commissioner has denied Allstate's requests for interim relief, in part on the ground that the factual submissions showed a hotly contested issue as to whether Allstate actually needed a rate increase. (Pet. App. 16). That ruling, which encompasses the issue of the Commissioner's power to issue interim relief under state law, is currently pending before the Superior Court, Appellate Division. To the extent that Allstate claims in fact that it has been deprived of a just rate of return, this claim is not ripe, because Allstate has not yet even extended coverage to the insureds at issue here and because its current rate increase petitions are still pending. See *MacDonald, Sommer & Frates v. County of Yolo*, 477 U.S. 340 (1986);

Williamson Planning Commission v. Hamilton Bank, 473 U.S. 172 (1985).*

Allstate's second point concerning an absolute right to protection against regulatory lag is equally lacking in merit. This Court has never held that there is a right to protection against all monetary losses due to delay in the regulatory process. Indeed in the *First English Evangelical Lutheran Church* case, on which Allstate relies (Petition at 20), wherein this Court ruled that state regulation which denies the use of property for a "considerable period of years" could constitute a taking, this Court carefully distinguished "the quite different questions that would arise in the case of normal delays in obtaining building permits, changes in zoning ordinances, variances and the like." 482 U.S. at 321. Plainly, a certain degree of delay in the rate adjustment process is simply a "necessary incident of rate regulation" which is an element of the risk associated with investment in a rate-regulated business. See *Public Util. Comm'n of Texas v. Pedernales Elec. Coop.*, 678 S.W.2d 214, 222 (Tex. Ct. App. 1984).

* Allstate's rate hearings are being held before independent administrative law judges, *N.J.S.A. 52:14F-1 et seq.* Allstate's hearing on a petition to raise its voluntary rates has concluded and the parties are awaiting the ALJ's initial decision after post-hearing submissions. The insurance statute, *N.J.S.A. 17:29A-14c(1)*, establishes a strict time frame for the issuance of the Commissioner's final order following receipt of the initial decision. A second hearing, on a petition to raise the rates to pass through certain surtaxes and assessments, is still pending before an ALJ. Allstate makes reference to this proceeding as "mired in discovery" (Pet. at 13); such delay is due to Allstate's refusal to cooperate with discovery requests from the Insurance Department's staff and Rate Counsel.

Indeed, it is well established that a regulation which controls rates, and by logical extension, a scheme which simply requires coverage of insureds at existing or higher rates, will be invalidated "on its face only if its terms preclude avoidance of confiscatory results." *Calfarm Ins. Co. v. Deukmejian*, 771 P.2d 1247, 1252 (Cal. 1989), citing *Pennell v. City of San Jose*, 485 U.S. 1 (1988); *Hutton Park Gardens v. Town Council*, 68 N.J. 543, 350 A.2d 1, 16 (1975). As this Court clearly held in *Maloney, supra*, a state may require an insurance company to cover customers that it would rather not insure:

The problem is a local one on which views will vary. We cannot say California went beyond permissible limits when it made the liability insurance business accept insurable risks which circumstances barred from insurance and hence from the highways. Appellant's business may of course be less prosperous as a result of the regulation. That diminution in value, however, has never mounted to the dignity of a taking in the constitutional sense. [*California Auto. Assoc. v. Maloney, supra*, 341 U.S. at 110-111].

Here, where Allstate has the option of charging these customers a higher rate even than its voluntary market rates, and where it has failed on the factual record to establish to the satisfaction of state appellate courts its need for interim rate relief, there is no constitutional violation and no need for review by this Court.

Finally, there is no significance to Allstate's claim (Petition at 20-21), that certiorari should be granted to resolve differences among state courts in dealing with various types of rate requests. It is well established that insurance regulation is uniquely a state concern. In fact,

Congress passed the McCarran-Ferguson Act, 15 U.S.C.A. §§1011-15 (1982), to ensure that states would be able to tailor their own individualized methods of regulating insurance companies in their states. See *Lac D'Amiante du Quebec v. American Home Assur.*, 864 F.2d 1033, 1039 (3d Cir. 1988), citing *Prudential Insurance Co. v. Benjamin*, 328 U.S. 408 (1946) ("Obviously Congress' purpose was broadly to give support to the existing and future state systems for regulating and taxing the business of insurance"). Given Congress' intention that the states act as "laboratories" in this regard, and this Court's well established rule that there is no one constitutionally required method of rate regulation, *Duquesne Light Co. v. Barasch*, *supra*; *F.P.C. v. Hope Natural Gas Co.*, 320 U.S. 591 (1944), it is not surprising that different states have reached different conclusions as to their requirements for rate regulation in their own jurisdictions. This result is not one of constitutional magnitude, was plainly within the contemplation of Congress, and does not require intervention or review by this Court. *Sup.Ct.R.* 10.1(b), (c).

In summary, it is clear that Allstate's petition requests this Court to intervene in an essentially fact-based rate dispute which is being properly handled by the Commissioner and the State's courts, in accordance with well established constitutional principles enunciated by this Court in its decisions. The petition should therefore be denied.

CONCLUSION

The petition in this case presents no issues of constitutional magnitude. Allstate has received judicial review of its claim to interim rate relief and has been denied such relief based upon the hotly contested factual record in this case. Moreover, Allstate's claim of an absolute right to protection against any financial loss due to regulatory lag is completely lacking in merit. Its facial challenge to the depopulation order must fail given the lack of conclusive factual proof that any such loss will occur. For all of these reasons, the petition for a writ of certiorari in this case should be denied.

Respectfully submitted,

ROBERT J. DEL TUFO
Attorney General of New Jersey
Attorney for Respondent
Samuel F. Fortunato,
Commissioner of Insurance of
the State of New Jersey

By: Susan L. Reisner
Deputy Attorney General
On the Brief
(Counsel of Record)

JOSEPH L. YANNOTTI
Assistant Attorney General
Of Counsel

DATED: January 16, 1992

APPENDIX 1

DOUGLAS S. EAKELEY
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UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

ALLSTATE INSURANCE)	
COMPANY,	)	Honorable
(an Illinois Corporation),	)	John W.
	)	Bissell
Plaintiff,)	
	)	Civil Action
v.	)	No. 90-1366
)	
JAMES J. FLORIO, in his	)	AFFIDAVIT
official capacity as Governor	)	OF
of the State of New Jersey	)	KAREN E.
and in his individual	)	MITCHELL
capacity; JASPER J. JACKSON,)	
in his official capacity)	
as Acting Commissioner of)	
Insurance of the State of)	
New Jersey; and ROBERT J.)	
DEL TUFO, in his official)	
capacity as Attorney General)	
of the State of New Jersey,)	
)	
Defendants.)	

KAREN E. MITCHELL, of full age, being duly sworn, according to law, upon her oath, says:

1. I am the Chief Examiner of the Department of Insurance of the State of New Jersey, Division of Financial Examinations. As such, I am responsible for examining the financial health of insurance companies operating in New Jersey. Part of that examination involves review of the Annual Statements filed with the Department by each company according to law. A review of a company's Annual Statement can reveal whether or not that company experienced an operating profit or loss during the year reflected in the Annual Statement.

2. I make and submit this Affidavit in response to Allstate's allegations of unprofitability in its Complaint, to the extent that the Court may deem it necessary to consider Allstate's factual contentions in disposing of the motions pending before it.

3. I have reviewed the 1988 and 1989 Annual Statements of Allstate Insurance Company. Contrary to what Allstate is alleging in this Complaint, it appears the company showed a profit on New Jersey private passenger automobile business in both 1988 and 1989. I must caution this Court that, with the exception of the "State Business Page" of the Annual Statement (page 14), no financial data filed in Annual Statements deals specifically and solely with the New Jersey part of a company's business unless the company writes business only in New Jersey. All Annual Statements reveal, on the State Business Page, the amounts of gross premiums written and earned, and total losses paid and incurred, in New Jersey. All other information contained in Annual Statements, including expenses and investment income, are reported as world-wide figures. Therefore, my analysis of

how well Allstate has performed on its private passenger automobile business in New Jersey is based in part on the actual figures on the State Business Page, and in part on estimated figures provided in the A.M. Best Aggregates and Averages Property and Casualty Manual. In making my calculation, I have taken the actual reported direct premiums earned from the State Business Page from Allstate's Annual Statements, and subtracted therefrom the actual losses paid and incurred on New Jersey business. I have further subtracted estimated loss adjustment and other expenses derived from applying industry-wide ratios as reported in A.M. Best to Allstate. Finally, I added estimated investment income similarly computed by applying A.M. Best ratios. My analysis is set forth in Exhibit A. It reveals that Allstate, in 1989, reported \$233,264,423 in earned premiums on New Jersey Private passenger automobile business, and \$185,145,357 in actual incurred losses.

4. The latter figure is an inflated calculation of incurred losses. It is inflated because it fails to deduct from those losses the amount of the incurred reimbursement to Allstate from the Unsatisfied Claim and Judgment Fund. Allstate, unlike most other companies, reports its actual incurred losses as including all monies advanced to claimants on behalf of the Unsatisfied Claim and Judgment Fund. ("UCJF" or "the Fund").

5. The Fund is organized by statute and its major function is to bear the cost of any individual's medical expenses resulting from any one accident to the extent those expenses exceed \$75,000. In other words, that individual's own insurance carrier is responsible for the first \$75,000 in medical expenses, and then the Fund is responsible. In practice the carriers continue to pay the insured's

medical expenses even when they exceed \$75,000, and then the carriers are reimbursed by the Fund for the amounts paid in excess of \$75,000. Thus at any given time, the books of a carrier in the auto insurance business will reflect an amount due from the Fund.

6. As a result of that reimbursement procedure, Allstate has set up its reported paid and incurred losses as *including* all medical expenses paid to any individual insured in excess of \$75,000 *without excluding* the amount reimbursed by the Fund. The Department is aware of this practice, since it is made evident by Allstate's inclusion, on Schedule F of its Annual Statement, of over \$111 million in money due to it from the Fund, as if the Fund was a reinsurer. Nothing on Schedule F is factored into reported paid and incurred losses on the State Business Page. Therefore, we know that the amount of incurred reimbursement from the Fund is *not* factored into Allstate's reported losses. This is inappropriate as a measure of determining whether a company made a profit. Clearly the amount of incurred reimbursement must be factored in order to arrive at a true picture of a company's profits.

7. After factoring that UCJF reimbursement in, Allstate's losses are reduced by over \$24 million in 1989, and also by over \$24 million in 1988. After subtracting estimated expenses and adding estimated investment income, Allstate shows an apparent 1989 profit on its private passenger automobile business of \$8,823,392, and an apparent 1988 profit of \$8,795,496. This results from only examining that *one* factor, treatment of Fund reimbursement. There are a multitude of other factors that, once verified, can alter the company's profit figure for each year. For example, Allstate reports a premium "ceded" to the Fund of over \$26 million on Schedule F.

No other company reports any such figure, and, I do not know the origin of that figure. The Fund obtains no "premiums", only "assessments," and the assessments are in no way as much as \$26 million. Until that figure is explained, my conclusion is a qualified one. The \$26 million reported "ceded" premiums *may* have an impact on Allstate's profit or loss in 1989 and in 1988. In addition, each profit figure may be higher or lower depending on how close the estimated expense and investment income figures are to the actual numbers. The Court should also be aware that these calculations do not account for the effect of reinsurance, which could also raise or lower the overall profit figure, depending on how successful Allstate was in reinsuring its losses. The financial data needed in order to make that analysis is not available, as mentioned above.

8. Finally, I note that my findings do not agree with the figures noted for Allstate in the Department's November 1989 "Insurer Profitability Report." The figures in that report were taken from insurance company records without independent verification by the Department. We now know that the figures contained therein relating to individual carriers' New Jersey performance may be totally inaccurate, as they are with respect to Allstate. Accordingly, the Department is working on amending that report to reflect independent analysis.

/s/ Karen E. Mitchell
Karen E. Mitchell

Sworn to and Subscribed
before me this 16th day
of May, 1990.

/s/ Stephen P. Tasy
Attorney-At-Law
State of New Jersey

EXHIBIT A

1989

	<u>No Fault & Liability</u>	<u>Physical Damage</u>	<u>Total</u>
Premiums			
Earned	\$147,660,175	\$85,604,248	\$233,264,423
*Losses			
Incurred	113,289,653	47,213,633	160,503,286
LAE Incurred	19,491,143	6,762,736	26,253,879
Other			
Underwriting Expenses	<u>35,528,925</u>	<u>18,532,481</u>	<u>54,061,406</u>
Total			
Expenses	\$168,309,721	72,508,849	240,818,570
Underwriting			
Gain (Loss)	(20,649,546)	13,095,399	(7,554,147)
Investment			
Income	14,323,037	2,054,502	16,377,539
Net Gain			
(Loss)	(6,326,509)	15,149,901	8,823,392

* Reported losses incurred	137,931,724	
UCJ reimbursement		13,746,161
Ending Balance UCJ		111,926,921
Beginning Balance	<u>101,031,011</u>	
Total	<u>113,289,653</u>	
(Incurred basis)		

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	<u>No Fault & Liability</u>	<u>Physical Damage</u>	<u>Total</u>
Premiums			
Earned	\$137,278,946	\$97,942,581	\$235,221,527
*Losses			
Incurred	112,964,490	49,951,416	162,915,906
LAE Incurred	18,120,821	7,737,464	25,858,285
Other			
Underwriting Expenses	<u>30,743,940</u>	<u>22,574,579</u>	<u>53,318,520</u>
Total			
Expenses	161,829,251	80,263,459	242,092,710
Underwriting			
Gain (Loss)	(24,550,305)	17,679,122	(6,871,183)
Investment			
Income	13,316,058	2,350,622	15,666,680
Net Gain			
(Loss)	(11,234,247)	20,029,744	8,795,496

* Reported losses incurred	\$137,389,274	
UCJ reimbursement		11,527,832
Pending Balance UCJ		101,031,011
Beginning Balance	<u>88,134,059</u>	
	<u>\$112,964,490</u>	

APPENDIX 2
STATE OF NEW JERSEY
DEPARTMENT OF INSURANCE

In The Matter of the Rate Application by Allstate
Insurance Company Dated October 15, 1990 Requesting
a +27.7% Increase in Private Passenger Automobile
Insurance Rates

OAL Docket No: INS 9536-90

NJDOI File No: 90-1320

Exhibit PT-1

Direct Pre-Filed Testimony and Exhibits of
Allan I. Schwartz

On Behalf of the
New Jersey Department of the Public Advocate
Division of Rate Counsel

January 25, 1991

In The Matter of the Rate Application by Allstate
Insurance Company Dated October 15, 1990 Requesting
a +27.7% Increase in Private Passenger Automobile
Insurance Rates

OAL Docket No: INS 9536-90: NJDOI File No: 90-1320

Direct Pre-Filed Testimony and Exhibits of Allan I.
Schwartz On Behalf of the New Jersey Department of
the Public Advocate

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V	Trend Period/Effective Date	12 - 15

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In The Matter of the Rate Application by Allstate
Insurance Company Dated October 15, 1990 Requesting
a +27.7% Increase in Private Passenger Automobile
Insurance Rates

OAL Docket No: INS 9536-90: NJDOI File No: 90-1320

Direct Pre-Filed Testimony and Exhibits of Allan I.
Schwartz On Behalf of the New Jersey Department of
the Public Advocate

List of Exhibits

<u>Exhibit Number</u>	<u>Description</u>
1	Summary of Rate Level Changes
2	Derivation of Rate Level Changes
3	Comparison of Overall Rate Level Indica- tions
4	Loss Development
5	Total Loss and Premium Trend Factors
6	Annual Loss Trend Factors
7	Fast Track Trend Data

- 8 FAIR Act Savings
- 9 Permissible Loss & Loss Expense Ratio
- 10 Underwriting Profit and Contingencies
- 11 Countrywide Residual Market Share
- 12 Data Bank Information on JUA Insureds
- 13 Allstate's N.J. Private Passenger Auto Profits

STATE OF NEW JERSEY
DEPARTMENT OF INSURANCE

In the Matter of the Rate	)	OAL Docket No:
Application by Allstate Insurance	)	INS 9536-90
Company Dated October 15, 1990)	
Requesting a +27.7% Increase in	)	NJDOI File No:
Private Passenger Automobile	)	90-1320
Insurance Rates)	

Direct Pre-Filed Testimony of Allan I. Schwartz On
Behalf of the New Jersey Public Advocate

I - QUALIFICATIONS

- 1. Q. Please state your name and address?
 - A. My name is Allan I. Schwartz. My address is 4400 Route 9 South, Freehold, New Jersey.
- 2. Q. By whom are you employed and in what capacity?
 - A. I am President of AIS Risk Consultants, an actuarial consulting firm which I started in November 1984. In that capacity I have performed

consulting work for a variety of clients covering a wide spectrum of actuarial projects.

3. Q. What was your previous employment history?

A. From May 1988 to January 1990 I was Assistant Commissioner with the New Jersey Department of Insurance (NJDOI). In that position, I was responsible for all property/liability filings, excluding workers' compensation, submitted to the NJDOI in addition to other responsibilities. From June 1986 until April 1988 I was Chief Actuary for the North Carolina Department of Insurance (NCDOI). I was responsible for all the actuarial work at the NCDOI, both property / liability and life / accident / health. From August 1977 to November 1984 I worked for the actuarial consulting firm of Woodward and Fondiller. My last position at that firm was Senior Actuary. Prior to that, from March 1976 to August 1977, I was employed by the National Council on Compensation Insurance (NCCI). While there, I worked on rate level analyses, benefit factor evaluations, and special projects. Before that, I attended college where I received a B.S. degree in physics from Cooper Union.

4. Q. Are you a member of any actuarial societies?

A. I am a Fellow of the Casualty Actuarial Society, an Associate in the Society of Actuaries, a Member of the American Academy of Actuaries, and a Fellow of the Conference of Actuaries in Public Practice. I have belonged to various regional actuarial organizations and professional actuarial committees. In addition, I served on the Property / Casualty and Life / Accident / Health Actuarial Task Forces of the National Association of Insurance Commissioners

(NAIC). I was also Chairperson of a sub-committee for the NAIC statistical task force. This sub-committee developed the current NAIC standard private passenger automobile statistical data reporting requirements.

5. Q. Would you please describe some of your additional professional activities?

A. I have written several papers dealing with various aspects of actuarial work. These have included topics on ratemaking, reserving, and reinsurance. I have also presented lectures and taught classes on these subjects. In addition, I was editor of Fresh Air Magazine, a newsletter published by Actuaries in Regulation. This is a special interest group of the Casualty Actuarial Society composed of actuaries who work for State Insurance Departments.

6. Q. Have you previously testified in regulatory proceedings regarding insurance rates

A. Yes. I have testified in property / liability insurance ratemaking proceedings in Arkansas, Maine, Massachusetts, North Carolina, Oklahoma, Rhode Island, South Carolina, Texas and Virginia. In addition, I have reviewed rate filings for the Insurance Departments in Delaware and New Jersey, which were resolved without a hearing.

7. Q. Do you have a resume setting forth your professional background?

A. Yes. It is included as an Appendix A to this testimony.

II - SUMMARY

8. Q. Have you reviewed the rate filing by Allstate Insurance Company (Allstate) dated October 15, 1990 requesting a +27.7% increase in private passenger automobile insurance rates, the additional information supplied in response to data requests, and other materials?

A. Yes. I have.

9. Q. What issues did you analyze in your study?

A. There were seven main items that impacted the overall premium level indication. These were the (1) loss development factors, (2) length of trend period / proposed effective date and annual trend factors, (3) impact of the FAIR Act, (4) consideration of the depopulation of the New Jersey Automobile Full Insurance Underwriting Association (NJAFIUA or JUA), (5) underwriting profit and contingency factors, (6) additional contingency loadings and (7) Market Transition Facility (MTF) operating results. The seven items and the impact they have on the private passenger automobile rate level are set forth in Exhibit AIS-3, Sheet 1. The differences in the treatment of these items between myself and Allstate is given descriptively in Exhibit AIS-3, Sheets 2 & 3.

In addition, Allstate included consideration of the premium surtax and Automobile Insurance Guaranty Fund Loan Assessment in its filing. It is my understanding that these issues are the subject of a separate proceeding. I have therefore not included the impact of these items on either the income or costs for Allstate.

Furthermore, I have included a discussion of Allstate's prior profitability for New Jersey private passenger automobile insurance and the Casualty Actuarial Society's Statement of Rate-making Principles. While these items do not impact the rate level directly, they do address some of the issues included by Allstate in its filing.

10. Q. What was the result of your analysis?

A. That the proposed rate increase by Allstate of +27.7% for private passenger automobile insurance will lead to excessive rates.

My indications are for an overall rate decrease of -11.4% for private passenger automobile insurance. This would be split as -11.4% for bodily injury (BI) liability, -22.2% for property damage (PD) liability, +8.5% for personal injury protection (PIP), +18.9% for uninsured motorists (UM), -19.9% for collision and -24.9% for comprehensive. These values are displayed in Exhibit AIS-1. The derivation of the rate level changes are set forth in Exhibit AIS-2, Sheets 1 to 6.

The seven items where I differ from Allstate are set forth in Exhibit AIS-3. The numeric values of these variables, as well as the impact on the rate level are set forth in Sheet 1. The differences are given in a descriptive manner in Sheets 2 & 3.

11. Q. Based upon your analysis, what is your recommendation regarding the needed private passenger automobile insurance rate level change for Allstate?

A. I would recommend that the overall rate level be decreased by -11.4% compared to the rates currently in place. Within this overall value,

some coverages (i.e., PIP and UM) would have the rates increase, while for other coverages (i.e., BI and PD liability along with physical damage - collision and comprehensive) rates would decrease.

* * *

APPENDIX 3

DOUGLAS S. EAKELEY
Acting Attorney General of New Jersey
Attorney for Respondent
R.J. Hughes Justice Complex
CN 112
Trenton, New Jersey 08625

By: Donald M. Parisi
Deputy Attorney General
(609) 984-0183

SUPERIOR COURT OF
NEW JERSEY APPELLATE
DIVISION DOCKET NO. A-

IN THE MATTER OF	)	<u>Civil Action</u>
THE ASSIGNMENT OF)	
EXPOSURES TO THE	)	AFFIDAVIT OF
AETNA CASUALTY AND	)	MARTIN ROSENBERG
SURETY COMPANY)	

MARTIN ROSENBERG, of full age, being duly sworn according to law, upon his oath deposes and says:

1. I am currently employed as an Assistant Commissioner, Property/Casualty Division, of the New Jersey Department of Insurance. I was appointed to my present position in 1990.

2. Since 1988 I have been responsible for supervising the units that analyze and approve/disapprove property and casualty rate filings. This includes private passenger automobile insurance.

3. Further details on my educational and employment history are listed on pages 1 and 2 of Exhibit A.

4. I have personally undertaken the review of Allstate's rate filing dated October 15, 1990. I am the sole actuary within the Department responsible for this review.

5. Attached as Exhibit A is my prefiled testimony in the ongoing Allstate rate hearing which began on February 6, 1991 in the Office of Administrative Law.

6. Allstate requests an overall increase in private passenger automobile insurance rates of 27.74% in its October 15, 1990 filing.

7. I concluded from my review of Allstate's filing that the data provided by Allstate did not support the request for an overall rate increase of 27.74%. Rather, I concluded that the rate indication developed from the data should be an overall decrease of 8.3% (see Exhibit A).

8. As part of my analysis of the Allstate filing I reviewed the effect of the "depopulation requirement" on the indicated rate need of Allstate.

9. I have concluded that Allstate needs no rate increase to compensate for the depopulation requirement. I explain my analysis fully on pages 17-20 of Exhibit A.

10. Subsequent to the filing of my direct testimony, Exhibit A, Liberty Mutual Insurance Company filed the type of standard/non-standard rating plan described on pages 17-19 of my testimony. This filing was made on February 1, 1991 and approved by the Commissioner on February 11, 1991.

11. Allstate has yet to file a standard/non-standard rating plan.

/s/ M. Rosenberg
Martin Rosenberg

Sworn to and subscribed
before me this 22 day
of February, 1991.

/s/ Donald I. Bryan, Jr.
Donald I. Bryan, Jr.
An Attorney at Law of New Jersey.

PETITION FILED
JAN 17 1992

In The
Supreme Court of the United States

October Term, 1991

ALLSTATE INSURANCE COMPANY,
an Illinois Corporation,

Petitioner,

v.

SAMUEL F. FORTUNATO,
Commissioner of Insurance of
The State of New Jersey,

Respondent.

On Petition For A Writ Of Certiorari To The
Appellate Division Of The Superior Court
Of The State Of New Jersey

MOTION FOR LEAVE TO FILE AND BRIEF AMICI
CURIAE OF THE NATIONAL ASSOCIATION OF
INDEPENDENT INSURERS, THE ASSOCIATION OF
CALIFORNIA INSURANCE COMPANIES, THE
INSURANCE FEDERATION OF MINNESOTA, THE
INSURANCE FEDERATION OF PENNSYLVANIA,
INC., AND THE WISCONSIN INSURANCE
ALLIANCE IN SUPPORT OF PETITIONER

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No. 91-983

In The
Supreme Court of the United States
October Term, 1991

ALLSTATE INSURANCE COMPANY,
an Illinois Corporation,

Petitioner,

v.

SAMUEL F. FORTUNATO,
Commissioner of Insurance of
The State of New Jersey,

Respondent.

On Petition For A Writ Of Certiorari To The
Appellate Division Of The Superior Court
Of The State Of New Jersey

MOTION FOR LEAVE TO FILE BRIEF AMICI CURIAE

Pursuant to Rule 37.4 of the Rules of this Court, The National Association of Independent Insurers ("NAII"), The Association of California Insurance Companies, The Insurance Federation of Minnesota, The Insurance Federation of Pennsylvania, Inc., and The Wisconsin Insurance Alliance hereby respectfully move for leave to file the attached brief *amici curiae* in support of petitioner Allstate Insurance Company. The consents of the petitioner and of respondents Aetna Casualty & Surety Company and

Colonial Penn Insurance Company have been obtained. The New Jersey Attorney General has withheld consent.

Movants are respectively a national and state insurance trade associations representing insurers throughout the United States.¹ The member companies of movants write a significant percentage of the automobile insurance policies issued annually in the United States. Thus, movants are vitally interested in the issue presented in this case – whether a satisfactory mechanism for interim relief and judicial review is afforded under a state statute regulating automobile insurance rates so as to protect fundamental constitutional rights and avoid the imposition of confiscatory rates.

In its brief, petitioner addresses the laws of the State of New Jersey and the direct impact of those laws and the decision below on petitioner. Movants seek to present this Court with a broad view of automobile insurance, state insurance regulation, and the impact of regulations and decisions such as the one at issue on the insurance industry and the nation as a whole. In addition, movants set forth in the attached brief decisions of state courts of last resort and federal courts which are in conflict with the decision below. Movants believe that the attached brief will assist the Court in understanding the importance of the issue presented in this case to the insurance industry

¹ Petitioner Allstate Insurance Company is a member company of all *amici* except The Wisconsin Insurance Alliance.

at large, and the necessity for action by this Court to address the significant constitutional issues raised herein.

WHEREFORE, *amici curiae* respectfully request that their motion for leave to file an *amici curiae* brief in support of petitioner be granted.

Dated: Norwich, Vermont
January 17, 1992

Respectfully submitted,

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STATEMENT OF INTEREST

The National Association of Independent Insurers ("NAII") is a national trade association representing the interests of over 560 property and casualty insurance companies. NAII member companies underwrite approximately 36% of the private automobile insurance in the United States. The Association of California Insurance Companies, the Insurance Federation of Minnesota, the Insurance Federation of Pennsylvania, Inc., and the Wisconsin Insurance Alliance ("Wisconsin") are state trade associations representing the interests of member insurers in their respective states. Allstate Insurance Company ("Allstate"), the petitioner, is a member company of all *amici* except Wisconsin.

The *amici* have a vital interest in the rate regulation of the automobile insurance industry by the states and the need for a mechanism for interim rate relief and judicial review to avoid the imposition of a confiscatory rate structure.

SUMMARY OF ARGUMENT

The insurance industry in the United States is facing a crisis. Insurers, experiencing increasing liabilities and unable to earn a fair rate of return, have been forced to withdraw from critical markets. Major insurer insolvencies have already been experienced and the threat of mounting insurer insolvencies is looming on the horizon. Congress and the state legislatures, as well as the state courts, have been grappling with various aspects of the problem. The crisis facing the insurance industry in general and the auto insurance industry in particular poses a difficult dilemma for government, the courts, industry and our society as a whole. The solutions are not self evident and they will take time and a great deal of effort to formulate and implement.

Amici do not presume to ask this Court to resolve or remedy this multi-faceted nationwide problem. But *amici* do believe that this Court's intervention is essential to

protect certain fundamental constitutional rights that are being violated, and to ensure that the American system of automobile insurance will not be destroyed, but will be able to continue, while the broader solutions to the overall problem evolve.

The necessity of relief from this Court arises out of efforts by state legislatures in recent years to implement a variety of mechanisms to depress automobile insurance rates, and in particular the sweeping legislation enacted by the State of New Jersey in 1990 following the election of Governor Jim Florio, entitled The Fair Automobile Insurance Reform Act of 1990 ("FAIRA").¹ The New Jersey legislation required assumption of enormous debt by insurers, elimination of various charges, and mandatory coverages, while at the same time purporting to guarantee to the insurers their constitutional right to an adequate rate of return.

The validity of the statute and its implementation, and the proposition that an adequate rate of return is in fact feasible under the statute, have been subject to extensive challenges, and numerous carriers have announced their intention to withdraw from the state as a result of the legislation. These challenges and withdrawals will be addressed in complex judicial and administrative hearings, which may take years to resolve. However, in the interim, by virtue of the decision below, the carriers are denied a viable mechanism for achieving an adequate and equitable return, should their challenges be sustained. Absent such a mechanism, any ultimate relief would only be prospective, and therefore illusory as to the periods that have passed, and the automobile insurance system may be destroyed in the meantime.

As Justice Garibaldi of the New Jersey Supreme Court observed in expressing her own doubts as to the denial of an earlier "facial" challenge to FAIRA:

Neither the insurance company not this state's insurance market will be adequately protected

¹ The Statute is reproduced in Appendix 7 to the Petition.

by the pyrrhic discovery after it has ceased doing business here (and perhaps elsewhere) that it deserved a rate increase five years ago.²

Nevertheless, when faced with an "an applied" challenge to FAIRA in the instant case, the New Jersey Court refused to act.

Thus, the issue presented by this case is whether a state can impose a regulatory system which is alleged to be confiscatory, without providing a viable timely mechanism for review, which will afford meaningful relief if the system is determined to be confiscatory. Other decisions in both federal and state courts have recognized the inherent danger and risks of such legislation and have taken steps to protect the carriers, the consumers and the overall insurance system, while these issues are being resolved. New Jersey statute and the decision of the New Jersey Court afford no such protection. They should not be permitted to stand.

It should be emphasized that the Petition challenges the validity of the statute as applied. It is the contention of the Petition that Allstate cannot be compelled by the application of the statute to write new business without first being afforded a viable mechanism to ensure adequate rates. The issues raised by the Petition are thus ripe for review by the Supreme Court.

ARGUMENT

I. The Importance of Insurance In General, and Automobile Insurance in Particular

As Professor (now Judge) Keeton has observed, "[i]nsurance is an important, and perhaps essential, aspect of the business and personal lives of the vast majority of individuals living in the United States."³

² *State Farm Mutual Auto. Ins. Co. v. State*, 124 N.J. 32, 68, 590 A.2d 191, 210 (1991) (Garibaldi J., concurring).

³ R. Keeton and A. Widiss, *Insurance Law, A Guide to Fundamental Principles, Legal Doctrines and Commercial Practices* 1 (1988).

Billions of dollars of private and commercial insurance coverage is written every year in the United States.⁴

Insurance is a method of managing and allocating risk by distributing it among large numbers of individuals or enterprises.⁵ The simple fact is that virtually every aspect of business and personal life entails some measure of the risk of injury or loss. Those risks are so significant that without a means of protection against such risks we could not function on an individual or societal basis. Insurance provides the means of protection by allocation of such risks, and insurance companies underwrite and manage that allocation of risk.⁶

The automobile, and automobile insurance, have played a particularly unique role in the development of the United States in the twentieth century. From the days of Henry Ford and the Model T, the automobile has been and even today remains the symbol of the American dream, the hallmark of American business and technology. The vast majority of American adults own or drive cars. The network of roads and highways crisscrossing the nation is unequalled throughout the world.

Yet, with the great success of the automobile came risks: risk of accident, risk of theft, risk of damage to the auto, and risk of serious injury and death to drivers, passengers and pedestrians. The American tort system, for better or for worse, has provided a mechanism for injured persons to recover for their injuries from auto accidents, recoveries which would far exceed the abilities to individuals or companies to pay on a personal basis. Automobile insurance has provided the means of compensating for automobile damage and injury and has

⁴ *Id.*

⁵ See K. Abraham, *Distributing Risk: Insurance Legal Theory and Public Policy* 1-2 (1986).

⁶ See generally *id.*

provided the means to tolerate the risks of the automobile, which is so important to our society. Thus, automobile insurance plays a critical role and function. If its ability to function is threatened, our modern American way of life is threatened.

II. Insurance Crises of the 80's and the 90's

In the 1980's the insurance industry and the public faced a crisis of insurance availability. Insurance was unavailable for many types of risks, *inter alia*, because underwriting of the 70's led to unanticipated losses, and insurers were unwilling or unable to commit their resources to underwriting similar risks in the early and mid 1980's.⁷ As a result, schools, day care centers, ect. closed because insurance was unavailable.⁸ This crisis was precipitated by economic and market forces, and towards the end of the 80's was showing signs of amelioration.⁹

However, the 90's is seeing the beginnings of a crisis of a different and much more ominous nature, the

⁷ See *In Re Insurance Antitrust Litigation*, 723 F. Supp. 464 (N.D. Cal. 1989), rev'd and remanded, 938 F.2d 919 (9th Cir. 1991); Priest, *The Current Insurance Crisis and Modern Tort Law*, 96 Yale L.J. 1521 (1987); Abraham, *Making Sense of the Liability Insurance Crisis*, 48 Ohio St. L.J. 399 (1987).

⁸ See Priest, *supra* note 7, at 1521-22; Gillies, *Managing the Market Regulating the Insurance Business*, 18 Brief 16 (1988) (A.B.A. Tort and Ins. Prac. Sec.); New York Times, March 28, 1986, at D16, col.1 (Congress "swamped" with warnings that small businesses are facing bankruptcy due to high cost and/or unavailability of liability insurance).

⁹ See New York Times, Feb. 16, 1987 § 1, at 12, col. 3 (Liability insurance crisis easing, with insurance becoming more available).

insolvency of major insurers and the forced withdrawal of insurers from the market place.¹⁰

This is due to many complex factors. Certainly, what turned out to be imprudent investments in real estate and junk bonds has been a contributing factor.¹¹ To some extent, this can be remedied by future investments strategies and controls.

However, what is of greater and perhaps the greatest concern, and of particular relevance here, is the forced withdrawal from the market place by insurers because they are subjected to a rating structure which prevents them from operating profitably, and indeed makes it inevitable that they will lose money, and the failure of the legislatures and the courts to provide adequate and timely means of review and redress. A free market economy cannot survive in such an environment.

This has been of particular and growing concern in the automobile insurance field.

¹⁰ In April of 1991, California regulators seized control of Executive Life Insurance Company, the largest failure of an insurer to date. *New York Times*, April 12, 1991, at A1, col. 6. Also seized in 1991 were First Capital Life Insurance Company, Monarch Life Insurance Company, and Mutual Benefit Life Insurance Company. *See New York Times*, July 19, 1991, at A1, col.1. *See also Trouble in Insurance City*, *Boston Globe*, Nov. 6, 1990, at 25p; *The Travelers Rides into the Storm*, *New York Times*, Dec. 2, 1990, § 6, part 2, at 13; *Will Insurance Industry Go the Way of S & L's?*, *Washington Post*, July 1, 1990, at H1; Subcomm. on Oversight and Investigations of Comm. on Energy and Commerce 101st Cong., 2d Sess., *Report on Insurance Company Insolvencies* (Comm. Print 1990) (John D. Dingell, Chairman). Figures on insolvencies of property and casualty insurers compiled by the National Conference of Insurance Guaranty Funds, the National Association of Insurance Commissioners, and A. M. Best Company for the years 1980-1991 are set forth in *Gastel, Insolvencies/Guaranty Funds*, Insurance Information Institute (1992) (available on NEXIS).

¹¹ *Id.*

III. Rate Regulation and Suppression of Auto Insurers in the 90's

Following the decision of this Court in *United States v. South-Eastern Underwriters Ass'n*, 322 U.S. 533 (1944) and the promulgation of the McCarran-Ferguson Act, 15 U.S.C. § 1011 *et seq.*, the following year, regulation of insurance was largely left to the states.

Automobile insurance has for at least two decades been perhaps the most heavily regulated of all forms of insurance by the states. This is due to the fact that the vast majority of adult Americans drive cars and that there is an inherent potential for serious accident and injury. Mandatory auto insurance laws, no-fault laws, and assigned risk plans implemented since the 1970's represent attempts by the states to make available the necessary coverages.¹²

In addition to the laws designed to ensure coverage, the states adopted a variety of approaches to regulate insurance rates. Historically, these included competitive systems where rates were set entirely by market forces,

¹² Twenty-four states adopted no-fault laws between 1970 and 1975. J. O'Connell, *The Lawsuit Lottery, Only the Lawyers Win* 158 (1979). Examples of no-fault statutes are N.Y. Ins. Law § 5101 *et seq.* (Consol. 1985); Mich. Comp. Laws Ann. § 500.3101 *et seq.* (West 1983); and Conn. Gen. Stat. Ann. § 38-319 *et seq.* (West 1987). For examples of mandatory insurance laws, see Ill. Ann. Stat. ch. 95 1/2 para. 7-601 (Smith-Hurd 1991) and Conn. Gen. Stat. Ann. § 38-327 (West 1987). Cal. Ins. Code § 11620 *et seq.* (West 1988) and Mich. Comp. Laws Ann. § 500.3301 *et seq.* (West 1983) are examples of assigned risk statutes.

For cases upholding these kinds of laws, see *Montgomery v. Daniels*, 38 N.Y.2d 41, 340 N.E.2d 444, 378 N.Y.S.2d 1 (1975) (upholding constitutionality of New York no-fault law); *Gentile v. Altermatt*, 169 Conn. 267, 363 A.2d 1, *appeal dismissed*, 423 U.S. 1041 (1976) (upholding Connecticut mandatory insurance law); *California State Auto. Ass'n Inter-Ins. Bureau v. Maloney*, 341 U.S. 105 (1951) (upholding California assigned risk statute).

with rates being filed with the state for information purposes only, as well as the so-called "prior approval" systems. However, even in the prior approval system, rates would generally become effective if not disapproved within a limited period such as 90 days. Other variations have included "file and use" and "flex" rating, which provided for immediate and automatic rate increases as needed.¹³

Under all these rate regulation systems, rates were set in what was essentially a free market system, subject to appropriate review by the states. Mechanisms existed for obtaining interim rate increases, and for expeditious review of administration and judicial rating decisions.¹⁴

However, beginning at the end of the 1980's with Proposition 103 in California, states through voter initiatives, political mandates or otherwise, took a new turn in implementing rate suppression mechanisms. Thus, in California under Proposition 103, an automatic 20% reduction in rates was required. Cal. Ins. Code § 1861.01 (West 1988). Similarly, in Pennsylvania, 1990 rates were rolled back to 1989 levels and frozen. 75 Pa. Cons. Stat. § 1799.7(b) & (d) (Supp. 1991). Nevada mandated a roll-back of the 1989-90 rates to a level 15% below the rates in effect on July 1, 1988. 1989 Nev. Stat. 784. In New Jersey under FAIRA, a reduction in charges was mandated, as was the absorption of an enormous debt from the Joint Underwriting Association and the mandatory assumption of coverages at reduced rates for thousands of drivers previously uninsurable in the voluntary market.¹⁵

¹³ For an explanation of historical rating systems, see Gastel, *Rate Regulation*, Insurance Information Institute, (1991); K. Abraham, *Insurance Law and Regulation* 104 (1988); see also O. Kramer, *Rate Suppression and its Consequences* (1991).

¹⁴ *Id.*

¹⁵ See FAIRA §§ 76, 78, N.J. Stat. Ann. 17:33B-49, 33B-51; FAIRA § 88 (c)(5), N.J. Stat. Ann. 17:33B-11(c)(5); additional details of FAIRA are provided in the Petition.

These rates suppression statutes have been subject to challenges on numerous grounds. *See Calfarm Ins. Co. v. Deukmejian*, 48 Cal.3d 805, 771 P.2d 1247, 258 Cal. Rptr. 161 (1989) (holding on due process and taking grounds that California statute prohibiting rate relief for first year unless an insurer was in danger of insolvency, was unconstitutional); *Guaranty Nat'l Ins. Co. v. Gates*, 916 F.2d 508 (9th Cir. 1990) (Nevada statute prohibiting inadequate rates nonetheless held unconstitutional because statute defined inadequate as guaranteeing only a break even return, not a constitutionally fair and reasonable return); *cf. Liberty Mutual Ins. Co. v. Jackson*, Civ. Action No. 90-961 (D.N.J. 1990); *Allstate Ins. Co. v. Florio*, Civ. Action No. 90-1366 (D.N.J. 1990) (challenges to FAIRA on impairment of contract and other grounds dismissed on the basis of abstention and tax injunction statute); *State Farm Mutual Auto. Ins. Co. v. State*, *supra*, 124 N.J. 32, 590 A.2d 191 (1991) (facial challenge to New Jersey statute dismissed); *Keystone Ins. Co. v. Foster*, 732 F. Supp. 36 (E.D. Pa. 1990) (rate freeze statute held not unconstitutional where rate relief was available in extraordinary circumstances).

The promulgation of these statutes was met with withdrawals of major carriers from critical markets.¹⁶

¹⁶ For example, Travelers has withdrawn from the California and Pennsylvania automobile insurance markets, and has also stopped offering automobile insurance in nine other states. *Los Angeles Times*, January 21, 1991, at D6, col. 1. *See Travelers Indem. Co. v. Gillespie*, 50 Cal. 3d 82, 785 P.2d 500, 266 Cal. Rptr. 117 (1990). Aetna Life & Casualty has withdrawn from Pennsylvania and South Carolina. 23 Executive Letter, Insurance Information Institute Nos. 20, 21 (May 14, 21, 1990). When Cigna Property and Casualty Company and St. Paul Company withdrew from the Massachusetts automobile insurance market, they followed twelve other insurers (including Petitioner) that had either left the Massachusetts market or had become insolvent since 1988. *Two More Car Insurers to Quit*

(Continued on following page)

Moreover, the withdrawals have escalated as carriers, who attempted to comply with the new statutes and regulations and at the same time earn an adequate rate of return, found they were unable to do so. This is best illustrated by the case of Allstate in New Jersey.¹⁷

The benefits of the rate suppression statutes are proving dubious at best. A lengthy study published in November 1991, by Orin Kramer, who previously headed New York Governor Cuomo's task force on the insurance liability crisis, concluded:

The central fallacy underlying rate suppression is the belief that it offers an economic free lunch: that if insurers are coerced into providing lower rates than would exist in a competitive pricing environment, other societal goals – insurance availability, service levels, accident protection, pricing equity and insurer solvency – will not suffer. The study documents that rate suppression buys short-term price relief to the detriment of those other policy objectives.¹⁸

In these circumstances, the ultimate outcome of the litigations and the economic and social benefits of the rate suppression statutes remain in serious doubt. While this is a matter of great concern to the industry, we recognize that these are issues which will be determined over time and in different forums.

The issue that is presented today, however, is whether or not the statutes *and* their implementation satisfy fundamental constitutional requirements.

(Continued from previous page)

State, Boston Globe, October 25, 1990, at 55p. A subsidiary of Hartford Insurance Company and others petitioned to withdraw from New Jersey upon promulgation of FAIRA. See *In The Matter of The "Plan For Orderly Withdrawal From New Jersey" of Twin City Fire Ins. Co.*, 248 N.J. Super. 616, 591, A.2d 1005 (App. Div. 1991).

¹⁷ See the Petition and the decision below.

¹⁸ O. Kramer, *supra* note 13, at ii.

As set forth above, in the *Calfarm* and *Gates* cases, the California Supreme Court and the Court of Appeals for the Ninth Circuit recognized that a rate suppression statute which was on its face confiscatory violates the Fourteenth Amendment. Thus, provisions of the California and Nevada statutes which permitted rate relief only in the case of insolvency, or permitted at most break even return, were found to be constitutionally impermissible.¹⁹

The New Jersey statute, which was clearly drafted with the California decision in mind, purported to overcome this problem by providing on its face that the insurers are entitled to earn an adequate rate of return.²⁰ However, where the New Jersey statute fails – and this is a more subtle and sinister infringement on constitutional guarantees – is that it does not provide adequate protection of the carriers' constitutional rights in its mechanisms for implementation. Thus, the statute as applied does not meet fundamental constitutional requirements.

IV. The Problem of the Unavailability of Interim Relief

In *Calfarm*, the California Supreme Court prudently stated "we focus less on the rate specified in the statute than on the ability of the seller to obtain relief if that rate proves confiscatory."²¹ Thus, the California Court recognized that while it is not the role of the courts in the first instance to determine the adequacy of the rates, it is the role of the courts to ensure that a mechanism exists for relief if the mandated rates are determined to be inadequate. The California Court went on to state "recognizing that virtually any law which sets prices may prove confiscatory in practice, courts have carefully scrutinized such

¹⁹ *Calfarm*, 48 Cal.3d at 821, 771 P.2d at 1255-56, 258 Cal. Rptr. at 169; *Gates*, 916 F.2d at 510.

²⁰ FAIRA §2(g), N.J. Stat. Ann. 17:33B-2(g).

²¹ *Calfarm*, 48 Cal.3d at 816, 771 P.2d at 1252, 258 Cal. Rptr. at 166.

provisions [for rate adjustment] to ensure that the sellers will have an adequate remedy for relief from confiscatory rates."²²

The problem with the New Jersey legislation, and with the decision of the New Jersey Court, is that while the statute pays lip service to the constitutional requirement that the carriers must earn a fair and reasonable return, it does not enable them to do so for the following reasons:

1. The statute does not provide for and the New Jersey courts have not permitted a satisfactory mechanism for an interim challenge to the adequacy of the rates set by the state administration agency or for judicial review of any such challenge. Disputes as to the adequacy of rates will thus take several years to resolve.

2. In the interim, carriers must take on thousands of new customers, who did not previously qualify in the voluntary market, at rates the carriers contend they have demonstrated to be *prima facie* confiscatory.²³

3. Even if the carriers wish to seek to withdraw from the market, as Allstate and others have been forced to, the process takes several years and they must take on new customers as well as continue with old customers at the rates they believe to be confiscatory.²⁴

4. No mechanism exists under FAIRA to recover losses for periods that have passed – which as set forth in the Petition, may be enormous – if in the end it is

²² *Id.* at 817, 771 P.2d at 1253, 258 Cal. Rptr. at 167. The *Calfarm* court also pointed out that "the terms 'fair and reasonable' and 'confiscatory' are antonyms, not separate tests." *Id.* at 816n.5, 771 P.2d at 1252n.5, 258 Cal. Rptr. at 166n.5 (citations omitted).

²³ FAIRA §88, N.J. Stat. Ann. 17:33B-11(c)(5).

²⁴ FAIRA §72, N.J. Stat. Ann. 17:33B-30; *see also* footnote 16, *supra*.

determined that the rates were not fair and reasonable and were in fact confiscatory.²⁵

Thus, despite the apparently benign language of the New Jersey statute that purports to guarantee an adequate rate of return, a structure has been set up under which, even if the carriers ultimately demonstrate that the rates are inadequate and confiscatory, they will be denied any possibility of recovery.

The carriers are effectively denied their day in court. Their property is being expropriated by the state without a meaningful opportunity for constitutional review.

The carriers cannot continue to exist and to provide the auto insurance that is vitally needed in this environment. Ironically, the very problem raised by the statute and the decision below was foreseen by Justice Garibaldi of the New Jersey Supreme Court in the decision rejecting the "facial challenge" to the constitutionality of the New Jersey statute in the *State Farm* case. Justice Garibaldi stated:

I concur in the Court's opinion [upholding the facial validity of the statute]. However, I write separately to emphasize that this statute is still susceptible to an as-applied challenge. I have grave doubts about the ability of the Commissioner of Insurance, under present regulations, to guarantee insurance companies a constitutionally-adequate rate of return. The present rate-making structure is lengthy and complex; the addition of the special separate-hearing procedure for rate relief will only add to existing delay. Although the length of time before rate relief is granted may not, alone, make the scheme constitutionally defective, *Helmsley v. Borough of Fort Lee*, 78 N.J. 200, 223, 394 A.2d 65

²⁵ New Jersey law does not permit recovery of losses resulting from inadequate rates through subsequent rate increases. In *Re Elizabethtown Water Co.*, 107 N.J. 440, 449-51, 527 A.2d 354, 359-60 (1987).

(1978), appeal dismissed, 440 U.S. 978, 99 S.Ct. 1782, 60 L.Ed.2d 237 (1979) the possibility for relief from confiscatory rates must be realistic. *Id.* at 226, 394 A.2d 65; *See also Calfarm Ins. Co. v. Deukmejian*, 48 Cal.3d 805, 817, 771, P.2d 1247, 1258, 258 Cal.Rptr. 161, 167 (1989) (court may strike down facially-valid law because procedures enacted under it "were so cumbersome and time-consuming that [affected persons] could not in reality obtain relief from confiscatory rates").

* * *

Current economic conditions compound my concerns. In the past, insurance companies, like banks, were always considered financial bulwarks. That is no longer true. *See Crenshaw*, "Personal Finance: Finding The Best Life Insurance; Buyers Must Consider Firm's Solvency As Well As Policy Cost," *Washington Post*, December 16, 1990, at H9 ("in the current economic uncertainty, the possibility [of an insurance company becoming insolvent] can no longer be overlooked"); *Floyd*, "Market Place: Failing Insurers' Bailout Cost Rises," *New York Times*, November 15, 1988, at D8 col. 3 (estimates of costs of saving failing insurance companies have soared from \$82,000,000 in 1984 to \$917,000,000 in 1987). Although the size of the accumulated unpaid debt of the Joint Underwriting Association is deplorable, the failure or withdrawal of insurance companies providing coverage in this state would prove even more damaging. Therefore, it is imperative that insurance companies actually receive a "fair and adequate rate of return" within a reasonable period of time. *Cf. Helmsley*, *supra*, 78 N.J. at 242, 394 A.2d 65 (holding that a more moderate regulatory scheme, *i.e.* one that does not attempt to keep investors' returns at the constitutional minimum, must be adopted where the governing body is not prepared to support a sophisticated

administrative relief system providing for prompt, fair and efficacious processes). Neither the insurance company nor this state's insurance market will be adequately protected by the pyrrhic discovery after it has ceased doing business here (and perhaps elsewhere) that it deserved a rate increase five years ago.²⁶

Notwithstanding her stated concerns, Justice Garibaldi concurred in the dismissal of the "facial" challenge in *State Farm*, so that the statute could be tested "as applied." The decision below provides the as applied challenge that Justice Garibaldi foresaw, and its circumstance parrots the very concern expressed by Justice Garibaldi. Nevertheless, notwithstanding Justice Garibaldi's opinion in *State Farm*, when again faced with this issue in the case of whether the statute as applied offered the necessary constitutional protection, the New Jersey Supreme Court declined review.

V. The Necessity For Review By the Supreme Court

The legislature and the courts of the State of New Jersey – operating in a highly charged political atmosphere – are not prepared to address the constitutional issues which have been raised. Their reticence to address these constitutional issues has created a split of authority between the courts and has exacerbated the insurance crisis.²⁷ Supreme Court review is particularly warranted in these circumstances.

Rule 10.1 of this Court indicates that the Court will particularly consider review of decisions on federal questions by state courts of last resort which conflict with

²⁶ *State Farm*, 124 N.J. at 66-68, 590 A.2d at 209-210.

²⁷ New Jersey seems content to ignore the mounting crisis, perhaps under the theory that carriers will not be forced into insolvency because they can offset their losses by charging higher rates in other states. This is the very argument that was rejected by the California court in *Calfarm*, 48 Cal.3d at 818-19, 771 P.2d at 1254, 258 Cal. Rptr. at 168.

decisions of other state courts of last resort or of federal courts of appeal. Here, the decision by the New Jersey Appellate Division (as adopted by the New Jersey Supreme Court in denying certiorari and dismissing the appeal) conflicts with the decisions of the California Supreme Court and the Ninth Circuit Court of Appeal on the question of whether interim relief must be afforded where rate suppression is claimed to be "temporary." This Court should accept this cases to resolve this conflict and protect important constitutional rights from being impaired or lost.

It is beyond dispute that under the takings clause of the 5th Amendment, where a state regulates an industry, it must nevertheless allow the affected businesses to obtain a "fair return" on their property in light of the risks borne.²⁸ Typical of the language of the pertinent cases is the requirement from *Duquesne* that courts scrutinize

what is a fair rate of return given the risks under a particularly rate setting system and . . . the amount of capital upon which the investors are entitled to earn that return.²⁹

Moreover, even a temporary "taking" offends the 5th Amendment.³⁰ Accordingly, since the 5th Amendment permits a "taking" only after due process of law, it will permit rate suppression only if there is an adequate mechanism to obtain relief from suppression which does not allow a fair return.

²⁸ *Duquesne Light Co. v. Barasch*, 488 U.S. 299 (1989); *FPC v. Hope Natural Gas Co.*, 320 U.S. 591 (1944); *Prendergast v. New York Tel. Co.*, 262 U.S. 43 (1923); *Tenaco Oil Co. v. Department of Consumer Affairs*, 876 F.2d 1013, 1029 (1st Cir. 1989).

²⁹ *Duquesne*, 488 U.S. at 310.

³⁰ *First English Evangelical Lutheran Church v. County of Los Angeles*, 482 U.S. 304 (1987); *Prendergast v. New York Tel. Co.*, 262 U.S. 43 (1923).

In cases of monopoly, it is sufficient to permit subsequent rate increases which will counterbalance the losses incurred in the period of suppressed, below-fair returns.³¹ However, where, as here, the adversely affected business is not a monopoly and it is not permitted to recoup its losses through future rate increases, the *only* procedural safeguard is a prompt, meaningful hearing. The California Supreme Court and the Ninth Circuit cases have upheld this procedural safeguard, but the instant decision of the New Jersey Appellate Division and Supreme Court departs from the rule and requires correction by this Court.

In *Calfarm*, after reciting that regulated companies have a right to obtain a reasonable return on their property, the California Supreme Court stated that the key it would focus on was "the ability of the [business] to obtain relief if that rate proves confiscatory."³² It held that Proposition 103 failed to provide a satisfactory relief mechanism because an insurer could seek relief under the scheme only where it would become insolvent as a result of the rates.³³ However, in ruling against the insurance commissioner,³⁴ the court also addressed, and squarely rejected, the commissioner's argument that the temporary character of the rollback obviated the constitutional requirement of procedural due process:

We recognize that emergency situations may require emergency measures. . . .

³¹ E.g., *Potomac Electric Power Co. v. Public Service Comm'n*, 380 A.2d 126 (D.C. 1977) (recoupment through future rate increase).

³² 48 Cal.3d at 816, 771 P.2d at 1252, 258 Cal. Rptr. at 166.

³³ *Id.* at 821, 771 P.2d at 1255-56, 258 Cal. Rptr. at 169.

³⁴ After severing the offending provision, the Court did uphold the remainder of the statute as providing an adequate mechanism for review – a timely mechanism which is not available under the New Jersey statutory scheme.

To justify a measure which deprives persons of a fair return, however, an emergency would have to be a temporary situation of such enormity that all individuals might reasonably be required to make sacrifices for the common weal. We do not believe that the circumstances which inspired Proposition 103 meet this requirement. . . . The asserted rise in insurance rates, rendering insurance unavailable or unaffordable to many, is not a temporary problem; it is a long term, chronic situation which will not be solved by compelling insurers to sell at less than a fair return for a year. *Over the long term the state must permit insurers a fair return; we do not perceive any short term conditions that would require depriving them of a fair return.*³⁵

Thus the California Supreme Court interpreted the taking clause as requiring a mechanism for addressing inadequate rates *even in the short term*.

The Ninth Circuit Court of Appeals reached the same result in the Nevada case concerning 1989 Nev. Stat. 784, which provided for a 15% rollback of auto insurance rates and a freeze at the level.³⁶ In a decision which carefully paralleled and discussed *Calfarm*, the court invalidated the Nevada statute as failing to guarantee the constitutionally required "fair and reasonable return."³⁷ The court cited with approval, and relied upon, the lengthy passage from *Calfarm* quoted above which rejected the purported justification of the lack of due process on the ground it was merely "temporary."

³⁵ *Id.* at 820-21, 771 P.2d at 1255, 258 Cal. Rptr. at 169 (emphasis added).

³⁶ *Guaranty Nat'l Ins. Co. v. Gates*, 916 F.2d 508 (9th Cir. 1990).

³⁷ *Id.* at 515.

By contrast, the New Jersey Supreme Court first rejected the "facial challenge" to FAIRA on the grounds that adequate review could be obtained through the administrative process,³⁸ but then inexplicably refused to hear the instant case which brought before it the "as applied" challenge when the administrative procedure failed to provide meaningful and timely relief.

With the rulings of the New Jersey Appellate Division and Supreme Court, there is now a direct conflict with *Calfarm* and *Gates*. The decision below approves as the ostensible due-process saving mechanism a process which could take several years to reach a determination³⁹ and which gives neither interim nor retroactive relief if the rates are shown by the lengthy process to be confiscatory. Thus it necessarily holds that the supposed temporary character – although lengthy – of the denial of due process is permissible. This result is in conflict and is incorrect.

Particularly as rate suppression statutes are mushrooming throughout the country, it is essential that the constitutional invalidity of these provisions be subject to proper scrutiny by the courts and that this scrutiny not be avoided and frustrated due to the absence of mechanisms for interim relief. The withdrawals and insolvencies that will inevitably follow if the validity of rate suppression statutes cannot be tested for years will have a devastating impact on the automobile insurance industry and its ability to underwrite risks.

The New Jersey situation poses a clear cut example of the abuse by a state of the rate regulation power. The Supreme Court is the last hope of the insurance industry, and the public it serves, to rectify this situation.

³⁸ *State Farm*, 124 N.J. 32, 63, 590 A.2d 191, 207 (1991).

³⁹ See Petition at 7; cf. Petition at 3-4n.5.

CONCLUSION

For the reasons set forth herein and in the Petition for a Writ of Certiorari, the Petition should be granted.

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In The
Supreme Court of the United States

October Term, 1991

ALLSTATE INSURANCE COMPANY,
an Illinois Corporation,

Petitioner,

v.

SAMUEL F. FORTUNATO,
Commissioner of Insurance of
The State of New Jersey,

Respondent.

Petition For A Writ Of Certiorari To The
Appellate Division Of The Superior Court Of The
State Of New Jersey

**PETITIONER'S REPLY AND SUPPLEMENTAL BRIEF
IN SUPPORT OF ITS PETITION FOR A
WRIT OF CERTIORARI**

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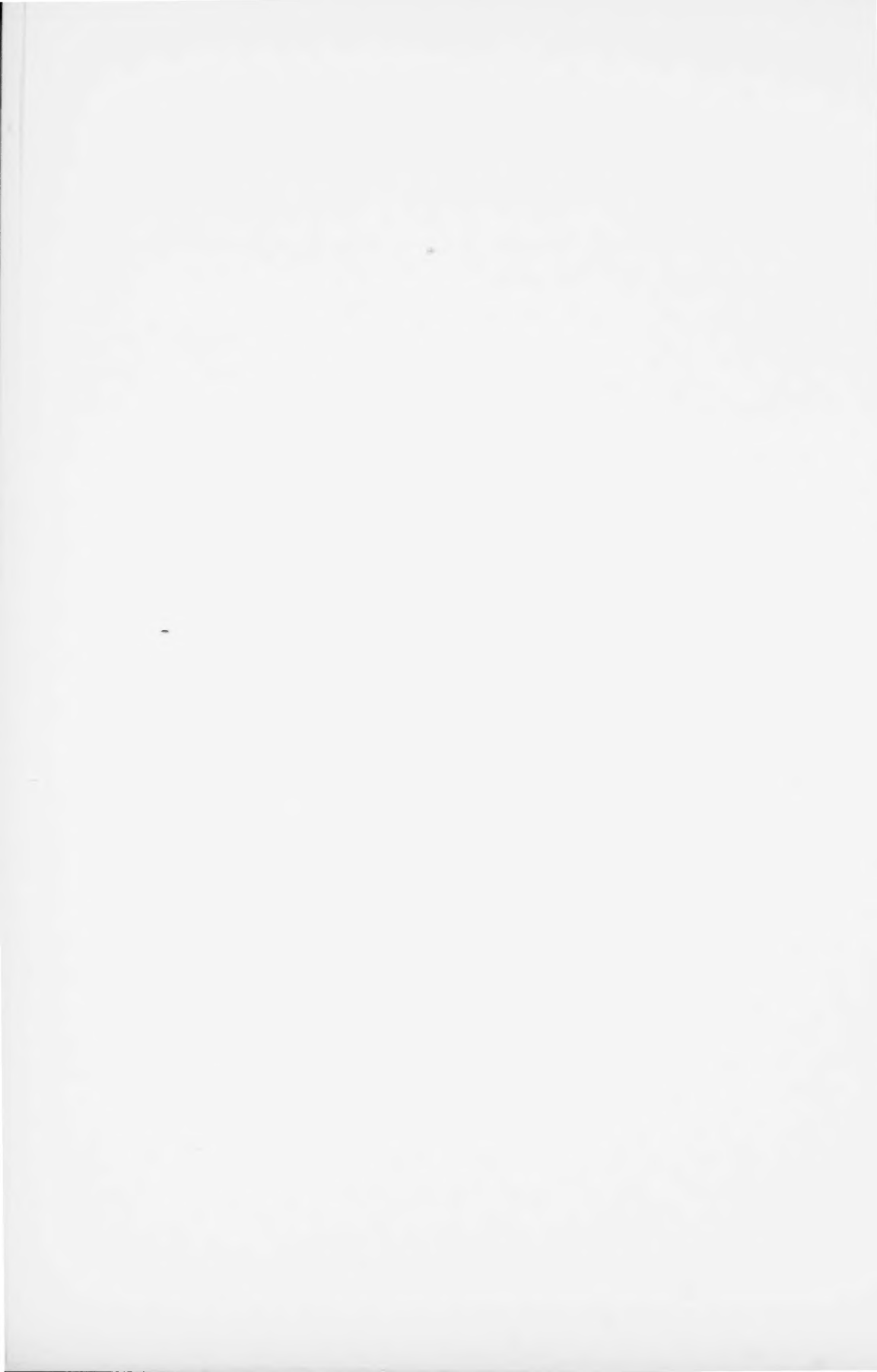
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**PETITIONER'S REPLY AND SUPPLEMENTAL BRIEF
IN SUPPORT OF ITS PETITION FOR A
WRIT OF CERTIORARI**

Allstate Insurance Company submits this combined reply and supplemental brief for two purposes: first, to update the Court on matters of import occurring since Allstate filed its original petition for certiorari; second, to correct the serious mischaracterization of Allstate's legal position in the Respondent's Brief in Opposition.

**I. RECENT EVENTS UNDERSCORE THE OUTRAGES
IN NEW JERSEY'S APPLICATION OF ITS SYSTEM
OF AUTOMOBILE INSURANCE RATE REGULA-
TION AND THE CONTINUING SIGNIFICANCE
OF THIS LITIGATION.**

For two years, New Jersey has sought to force Allstate and other insurance carriers to take over the business previously lodged with its State-operated JUA, whose inadequate pricing created a deficit of over \$3 billion dollars between 1983 and 1990. To this end, New Jersey required all carriers to take a portion of the old JUA business, now lodged in the MTF, without any advance determination that the rates set by the State would allow insurers to earn a constitutionally protected return.

Allstate asks this Court to compel New Jersey to provide at least preliminary judicial review of the adequacy of the rates for depopulation risks before compelling Allstate to insure those risks. Judicially noticeable documents (Pet. 17 n.15) show that these events occurred after filing of the Petition.

(1) On December 31, 1991, the Commissioner reissued the Depopulation Order. (Pet. Supp. App. 91-114) As modified by a new statute (Pet. Supp. App. 74-90), this Order is substantively similar to the original order, and requires Allstate to offer policies to successive groups of MTF insureds through February, 1993. Allstate intends to appeal from this Order and has sought a stay.

(2) On December 20, 1991, the Commissioner approved only a 14.9% increase in MTF rates, an amount his own actuaries admit will be inadequate for future MTF business. (Pet. Supp. App. 1-21) An appeal of this decision is pending; interim relief was denied without passing upon any facts relating to rate adequacy (Pet. Supp. App. 22-27) A further 16.8% increase in MTF rates is proposed. (Pet. Supp. App. 28-52) Yet, even if granted, this increase still leaves the MTF rates inadequate for the risks the Depopulation Order requires Allstate to assume. (Pet 18-19 n. 17)

(3) The Commissioner's actuaries have now reported that the MTF's former rates (at which the original Depopulation Order required Allstate to issue policies) produced a \$375 million loss during the MTF's first year of operation. (Pet. Supp. App. 53-56) Of this amount, \$180 million would have fallen on Allstate and other insurers had they insured sufficient depopulation risks at MTF rates. (Pet. Supp. App. 68) The Commissioner proposes to amend the MTF Plan of Operation to assess this portion of the MTF loss against Allstate and other insurers with depopulation shortfalls, while precluding them from including that assessment in any future rate filing. (Pet. Supp. App. 57-73, 115-116) Allstate's share of this penalty assessment would be over \$30 million. (Pet. Supp. App. 69)

Thus, Allstate now faces a revived order to insure depopulation risks, still without any opportunity to obtain prior judicial review of the adequacy of the rates permitted for that business. Moreover, it faces an unrecoverable assessment exceeding \$30 million based on its past failure to depopulate without access to such review.¹

¹ The fact that the assessment is to be unrecoverable necessarily assumes that Allstate's past failure to depopulate was wrongful. But, in light of the now indisputable inadequacy of the MTF rates, Allstate would surely have been protected

Additionally, absent fortuitous delay in revising this order pursuant to the Appellate Division's decision, Allstate would long ago have had to insure depopulation risks at rates now known to be inadequate. This both underscores the need for preliminary relief and shows this to be a controversy "capable of repetition, yet evading review." See *Southern Pacific Terminal Co. v. ICC*, 219 U.S. 498, 515 (1911).

II. NEW JERSEY CONTINUES TO SUBJECT ALLSTATE TO ITS CONFISCATORY REGIME OF REGULATION WITHOUT ANY PRIOR JUDICIAL DETERMINATION OF THE CONSTITUTIONALITY OF ITS RATES.

Allstate's Petition presents this Court with an important question of constitutional principle: does due process require some *advance* judicial review of the constitutional adequacy of rates for new business that the State forces upon a regulated firm. Allstate's claim is modest: it asks only that the State not be allowed to force it to assume extensive liabilities without some prior judicial review of the facts on rate adequacy comparable to the preliminary injunction proceedings which are available to protect against irreparable infringement of other constitutional rights. New Jersey concedes that its ratemaking procedures are subject to constitutional limits, but insists

(Continued from previous page)

against any depopulation obligation had it been granted the procedural protections it seeks here. Thus, if Allstate was entitled to those protections, its refusal to depopulate without them was not wrongful, and New Jersey is not free to penalize it. Because the Commissioner now seeks to penalize Allstate for its past failures to depopulate at inadequate rates, even an order prospectively allowing adequate rates for depopulation risks would not eliminate the controversy here. See, e.g., *Southern Pacific Co. v. ICC*, 219 U.S. 433, 452 (1911) (continuing collateral consequences of expired order preclude mootness).

that this case involves only "hotly contested factual issues" unworthy of this Court's review. (Br. in Opp. 9)

New Jersey is wrong. Its conduct throughout this massive and unfortunate litigation has honored the requirements of the just compensation clause only in the breach. The litigation nightmare that has followed since the passage of the New Jersey Fair Automobile Insurance Reform Act ("FAIRA") has arisen precisely because New Jersey has exploited the absence of effective judicial review during protracted and proliferating administrative proceedings to violate every principle of due process and just compensation law in order to wring the last cent out of Allstate and other insurance carriers held captive by its laws within the State.

The Commissioner asserts that Allstate has already received judicial review of rate adequacy and is simply unhappy with the result. However, *the Appellate Division could not have based its decision on the probable inaccuracy of Allstate's showing of a confiscatory effect because the Commissioner had not assembled any record which could support his alleged disbelief in that effect.*² Nor did the Appellate

² Allstate's evidence of MTF rate inadequacy was contradicted: Allstate actuaries, actuaries retained by the MTF actuarial committee, the Commissioner's own actuaries and regulatory presumptions all agreed. (Pet. 29-30; Pet. App. A-187A to -227A, A-140A to -144A) Recent developments have confirmed that showing. (Pet. App. A-312 to -337; Pet. Supp. App. 28-56) The facts which the Commissioner did dispute related to Allstate's "voluntary market" rates and his affidavits, even if taken as true, did not rebut Allstate's prima facie case of confiscation. Some of those facts (Br. in Opp. A-1 to -7) related only to rates for past years, whose adequacy or inadequacy cannot affect current rate levels. Others (Br. in Opp. A-16 to -18) would indicate some current excess profits, but would not show enough such profits to offset the undisputed MTF losses. Moreover, were Allstate realizing excessive profits in New Jersey, it obviously would not be withdrawing.

Division purport to resolve, even preliminarily, the issue of whether the Depopulation Order would have a confiscatory effect. Rather, it emphasized its inability to do so. (Pet. App. A-62 to -64)

To allow the Commissioner to transform the inability to review his action into a judicial endorsement of that action would create a blueprint for States to confiscate property at will, and without any possibility of prevention, so long as they arrange a suitably protracted administrative process whose completion is a precondition to judicial review.

The lack of an adequate record was not Allstate's fault. It presented *prima facie* proof to the Commissioner on a motion to stay, and he could have marshalled any contrary evidence and conducted proceedings (similar to a preliminary injunction hearing) to test the respective cases and reach a judicially reviewable conclusion as to the probable facts. *Instead, both the Commissioner and the courts refused to create or require an appropriate record and then denied relief to Allstate based on the record's inadequacies.* That is not due process.

Even if the Depopulation Order was a matter of urgency which could not be delayed for evidentiary proceedings (a fact belied by the subsequent seven-month delay in revising it to conform to the Appellate Division decision), there was a third alternative; provisional rate relief, subject to refund, pending further proceedings. *See, e.g., Prendergast v. New York Telephone Co.*, 262 U.S. 43 (1923). Sensitive administration of such a power (under standards similar to those for preliminary injunctions) would enable New Jersey to reconcile the objectives of preventing possible confiscation, conducting orderly and complete administrative proceedings, and promptly addressing urgent public problems. New Jersey should not be permitted to forego such reconciliation (by refusing to provide for provisional rates) at the cost of irreparable injury to Allstate's constitutional rights.

III. THE BASIC STRUCTURE OF NEW JERSEY RATE REGULATION REQUIRES CLOSE JUDICIAL SCRUTINY.

Several features of the New Jersey insurance rate regulation system call for special attention by this Court to the need to protect insurers subject to that system.

(1) ALLSTATE IS NOT IN A VOLUNTARY MARKET. The repeated reference to the "voluntary" market in the Commissioner's brief (Br. in Opp. i, 1, 4, 5, 12) is blatantly hypocritical. New Jersey law requires automobile insurers to continue insuring in perpetuity virtually all their existing customers, to take on enormous additional volumes of depopulation business to which they object, and (effective April 1, 1992) to accept all applicants (except a small percentage of drivers with records so bad that they are statutorily consigned to an assigned risk plan). An insurer has no power to set its own rates. Allstate is a conscript, not a volunteer.

(2) ALLSTATE HAS NO EXIT RIGHT. Despite Allstate's request to cease doing business in New Jersey, FAIRA and the Commissioner require Allstate to continue writing New Jersey automobile insurance (and to substantially increase its business volume) for many years hence. In addition, the Commissioner requires Allstate, as a condition of such cessation, to surrender all licenses to write other (historically profitable) lines of business in the State.

Allstate would willingly forfeit all its licenses; willingly suffer the loss of its good will, its physical plant, and its established organization in New Jersey; and willingly bear the heavy costs of unraveling its business and property arrangements within the State, solely in order to escape oppressive regulation under FAIRA. It seeks to do this as rapidly as possible, consistent with responsible treatment of current policyholders. But New Jersey insists that it stay.

New Jersey's decision to deny automobile insurers the right of exit speaks volumes about whether New Jersey's procedures can or will allow Allstate to recover

its constitutionally protected return on its investment. The State argues that a firm may be required to take a loss on one line of business if it can recoup that loss on another line.³ Accepting that premise *arguendo*, recoupment is somewhat protected where the exit right is in place, because the firm can leave if it is not able to realize a satisfactory rate of return on its entire line of business. But once the exit right is extinguished, there is no private counterweight to oppressive government regulation. Thus, strong procedural protections are even more necessary to preserve the constitutional right to a fair return.

(3) THE BURDEN OF NEW JERSEY'S REGULATORY SCHEME IS BORNE BY RESIDENTS OF OTHER STATES, WHO HAVE NO VOICE IN ITS POLITICAL PROCESS. When New Jersey decided to operate the JUA, the burden of subsidizing its losses was to fall on its citizens. By insisting that private companies take over the JUA's debt and its money-losing business, New Jersey has exported this burden, for Allstate must dedicate income and capital generated outside New Jersey to offset the State-created losses in New Jersey. This expropriation of out-of-state values again calls for closer scrutiny.

IV. UNWARRANTED "REGULATORY LAG" CANNOT JUSTIFY THE DEPRIVATION OF DUE PROCESS.

New Jersey justifies its dilatory practices by pointing to the inevitable level of "lag" that is built into any

³ The State's cases involve monopolies. The highly competitive automobile insurance industry involves no opportunity for monopoly profits and no opportunity to realize cross-subsidies. Hence, the State's system of regulation in this area must be subject to closer scrutiny to assure that the regulated party is allowed the return on investment constitutionally required. Under a system of purely prospective rate-making, such supervision is only possible if the rates for compulsory new business are judicially reviewable, at least on a preliminary basis, *before* the regulated company must undertake the business.

regulatory system. (Br. in-Opp. at 11). But New Jersey has raised regulatory lag to a new art form. It has done all in its power to slow the process of ratemaking in order to postpone the day of final reckoning, while claiming that judicial review is inappropriate because no final determination has been made regarding Allstate's overall rate needs.⁴

By spinning out endless procedural delays, the Commissioner is able to stonewall the courts and to conscript Allstate into writing as much business at as large a loss for as long a time as it can. New Jersey's policy of denying justice by delaying it violates the most elementary standards of due process. Such dilatory tactics or even cries of unavoidable delay cannot be allowed to seriously impair substantive rights, much less those protected by the Constitution.⁵

⁴ For example, though the FAIRA taxes and assessments have now been in effect for almost two years, Allstate's August, 1990 rate filing, which seeks to cover those costs, is still mired in pre-hearing discovery, with the Commissioner continually making demands which Allstate finds oppressive and, in some instances, impossible to satisfy. Similarly, the record of the hearing on Allstate's October, 1990 filing for its other rate needs was not closed to post-hearing submissions until January 31, 1992. Under statutory timetables, a decision by the Commissioner on the latter filing is therefore not due until approximately May 1, 1992, over 18 months after the rate filing.

⁵ See, e.g., *Smith v. Illinois Bell Telephone Co.*, 270 U.S. 587, 591 (1926) ("[p]roperty may be as effectively taken by long-continued and unreasonable delay in putting an end to confiscatory rates as by an express affirmance of them"); *Cutler v. Hayes*, 818 F.2d 879, 898 (D.C. Cir. 1987) ("if an agency's failure to proceed expeditiously will result in harm or substantial nullification of a right conferred by statute, 'the courts must act to make certain that what can be done is done'"); *Vitek Electronics, Inc. v. N.L.R.B.*, 763 F.2d 561, 568 (3d Cir. 1985)

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The Commissioner erects a straw man by asserting that Allstate demands "an absolute right to protection against regulatory lag" in adjusting the rates Allstate is permitted to charge. (Br. in Opp. 13) He cites cases saying that "a certain degree of delay in the rate adjustment process is simply a 'necessary incident of rate regulation' which is an element of the risk associated with investment in a rate regulated business." (Br. in Opp. 13)

But the Commissioner's caselaw concerns rate adjustment to take account of changing economic conditions. There, a regulated party can reasonably be expected to monitor conditions, anticipate the need for rate adjustment sometime before the need becomes acute, and request relief when there is still a reasonable period to process the request before the existing rates will impose substantial and irreparable harm.

Here, by contrast, the need for such relief stems from a new regulatory requirement, *so the State itself is responsible both for creating the rate inadequacy and for preventing rate adjustments*. This sort of regulatory lag is *not* an inherent risk of the regulated business. Rather, it is a loophole which could allow deliberate and unpreventable confiscation. Accordingly, preliminary judicial review *must* be available before implementation of a new requirement if a *prima facie* case of confiscation is presented. (Future cases can consider whether some similar requirement applies to cases where regulatory lag delays rate adjustments necessary to respond to changes external to the regulatory system.)

In any event, Allstate emphasizes that it is *not* demanding *absolute* protection against the effects of regulatory lag in rate adjustment. A full rate proceeding need not be completed before new regulatory requirements can

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(refusing to remand a case for further administrative hearings because administrative delay might frustrate substantive rights).

be imposed. Allstate claims only the right to *preliminary* judicial review of the rate impact and *provisional* rate relief (subject to refund) if appropriate to avoid an unjustified risk of irreparable confiscatory impact. Such protection is extended in other circumstances where State action threatens irreparable harm to constitutional rights. It is also required here.⁶

CONCLUSION

For all the reasons set forth herein and in the Petition, this Court should grant a writ of certiorari.

Respectfully submitted,

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⁶ The Commissioner also suggests (Br. in Opp. 12) that the pendency of proceedings seeking a rate increase means that Allstate's claim is not yet ripe. But, unlike the cases the Commissioner cites, this is not a case where existence of a taking depends on what use of realty will be permitted, while further administrative proceedings are necessary to determine what uses are permissible. Here, the order requiring Allstate to employ its property to insure depopulation risks is a *per se* taking. (Pet. 22-23) And, unless another order intervenes, Allstate must soon insure depopulation risks at *prima facie* inadequate rates; the resulting loss cannot be recovered through future charges.

ORDER NO.: A91-344

STATE OF NEW JERSEY
DEPARTMENT OF INSURANCE

IN THE MATTER OF THE)
DECEMBER 4, 1991 INTERIM) DECISION
RATE FILING BY THE MARKET) AND
TRANSITION FACILITY OF) ORDER
NEW JERSEY)

This matter has come before the Commissioner of Insurance (Commissioner) pursuant to: *N.J.S.A. 17:1C-6, 17:33B-11*; the decision of the Superior Court of New Jersey, Appellate Division, *In the Matter of the Commissioner of Insurance's May 10, 1991 Orders Regarding the January 17, 1991 Rate Filing by the Market Transition Facility of New Jersey*, (Docket No. A-4634-90T5, decided November 19, 1991) (hereinafter cited as *In re: Rate Filing by MTF*); and all powers expressed or implied therein; and upon the filing for an interim rate increase submitted by R.T. Haskins, Special Deputy Commissioner and Chief Operating Officer of the Market Transition Facility of New Jersey (MTF).

The MTF was created by statute as a mechanism to provide residual market automobile insurance coverage to bridge the gap between coverage provided through the New Jersey Automobile Full Insurance Underwriting Association (JUA) and a new assigned risk plan. *N.J.S.A. 17:33B-11*. Its creation was included among the comprehensive reforms to personal automobile insurance set forth in the Fair Automobile Insurance Reform Act of 1990, P.L. 1990 c.8 (*N.J.S.A. 17:33B-1 et seq.*) (FAIR Act). The MTF is to arrange for the issuance and renewal of

automobile insurance policies to those who cannot obtain coverage through normal market channels for the period from October 1, 1990 through September 30, 1992, after which it will be supplanted by an assigned risk plan to be created pursuant to N.J.S.A. 17:29D-1.

Initially, the rates charged by the MTF were based on those of its predecessor, the JUA, pursuant to N.J.S.A. 17:33B-11c(2). These rates had been raised approximately 10.3% effective October 1, 1990. On January 17, 1991 the MTF made a filing that requested higher rates. This request for increased rates was granted in part by the Commissioner by Order No. A91-212, issued May 10, 1991, to be effective for policies issued and renewed on and after June 15, 1991. Contemporaneously, the Commissioner issued Order No. A91-211, which denied an application by Allstate Insurance Company (Allstate), a personal automobile insurer with a significant share of the market, to participate in the MTF's rate change proceedings.

Allstate appealed both Orders to the Superior Court, Appellate Division, which issued its decision November 19, 1991. *In re: Rate Filing by MTF*, supra. The Court reversed the Order excluding Allstate from the MTF rate setting process finding that the Commissioner was obligated to establish procedures for the fixing of MTF rates which provided interested parties with an opportunity to participate. It directed the Commissioner to take immediate action to set proper MTF rates and stated: "We order the Commissioner to meet with representatives of interested parties within 15 days of this opinion to fix a manner and a time schedule for the accomplishment of

the purposes identified in this opinion." *In re: Rate Filing by MTF*, slip opinion at 23.

On November 25, 1991, the Commissioner issued Bulletin 91-20 which set the meeting for December 4, 1991. On November 26, 1991, the Commissioner issued Bulletin 91-21 which included two documents for discussion at the December 4, 1991 meeting as follows:

1. A document entitled "Rate Proposal Procedures for the MTF" which was proposed as an amendment to the MTF Plan of Operation; and
2. A second document entitled "Interim Rate Proposal Procedures for the MTF," which was intended to respond promptly to the Court's directive.

On December 4, 1991, Special Deputy Commissioner Haskins filed on behalf of the MTF an application for an interim rate increase, which is the subject of this Decision and Order. The MTF's interim rate filing was announced at the December 4, 1991 meeting of interested parties (Transcript, p.8) and copies were distributed to those attending. In announcing the interim rate increase filing, Special Deputy Commissioner Haskins noted that preliminary data indicated an MTF deficit of approximately \$300 million for its first year of operation (Transcript, p. 11).

In discussing the proposed interim rate increase at the December 4 meeting, Special Deputy Commissioner Haskins reported that the application was made based upon preliminary data which estimated a required rate increase in the range from 15 to 45 percent. (Transcript, p. 11). He noted that the data was incomplete in that it did

not include any information for September 1991, and did not include complete data for the calculation of "incurred but not reported" (IBNR) losses. (Transcript, pp. 11-12). The interim rate filing requested a 15 percent overall increase, at the low end of the range, which was to be followed by an additional rate increase application to meet the MTF's ultimate rate need. This additional rate increase application would be filed pursuant to the procedures proposed for the MTF Plan of Operation as soon as complete data were available later this month. Special Deputy Commissioner Haskins reported that the interim rate change proposal, to be followed by a further request based on complete data, was supported by a majority of the members of the MTF Advisory Committee. (Transcript, p.13).

The interim rate increase application consists of a cover letter summarizing the requested increase, a rate proposal consisting of five pages (including exhibits) and a Report of Rate Level Indication Analysis from O'Neil Consulting Services, the MTF's consulting actuary dated December 3, 1991 (OCS Report). The application proposes a 22 percent increase on liability coverages, which will result in an overall revenue increase of 15 percent for the MTF.

Several representatives of interested parties commented at the December 4, 1991 meeting. Lauren Townsend, representing New Jersey Citizen Action (a consumer coalition) urged that MTF rate change procedures provide for public hearings be held at times more accessible for New Jersey drivers, and that MTF rate applications be subjected to scrutiny by actuaries independent of the insurance industry. (Transcript, pp.42-45). Martin Brown,

representing State Farm Mutual Automobile Insurance Company (State Farm) stated that State Farm will file written comments on the technical aspects of the procedures and urged that the interim rates be implemented as soon as possible. State Farm further urged that MTF financial information be made available as promptly as possible, noting that State Farm's share of the market may make it responsible for a significant amount of any deficit. State Farm further urged that the Department should consider promulgation of administrative rules for the retirement of that debt through a recoupment mechanism, and not necessarily through a loading into MTF rates. (Transcript, pp. 45-47).

Mark Allaben, a member of the MTF Advisory Committee representing Travelers Insurance Companies, stated his support for the interim rate increase as "a small, good step forward to getting the MTF back to a break even position." (Transcript, pp. 47-48).

David Snyder, representing the American Insurance Association (AIA), commented on the significance of the expected MTF deficit, and on the importance of knowing a final date for a decision on the proposed rate change. Secondly, he noted that it was important to determine how IBNR losses are dealt with in the filing *because they can account for as much as one third of ultimate losses*. He further indicated that attempting to establish rates without IBNR would "violate every conceivable principle of actuarial science." He also urged that the books of the MTF be open to interested insurers and members of the public. AIA further requested that the rate filing include "some explanation of how the companies will be able to recover" the deficit.

Steve Carrellas, representing the National Motorist Association, requested that the procedures for reviewing MTF rate proposals include additional time for written public comments and a process for obtaining documents. He further expressed his concern that the drivers remaining in the residual market would be responsible for payment of any deficit already accrued. (Transcript, pp. 51-55).

Ed McCool, Executive Director of New Jersey Common Cause, inquired about the role of the Public Advocate in reviewing MTF rates. He urged that any MTF rate change proposal consider the expected effects of cost savings under the FAIR Act and urged that "good drivers" in the MTF (that is, drivers with no accrued automobile insurance eligibility points, see *N.J.A.C.* 11:3-34) be spared any rate increase. He suggested that any increase in MTF rates be delayed until after April 1, 1992 when eligible persons could freely obtain automobile insurance in the voluntary market. (Transcript, pp. 59-73).

Larry Johnson, representing The Chubb Group of Insurance Companies (Chubb) commented that Chubb's actuarial consultant had estimated the existing MTF deficit in excess of \$450 million, and that an additional \$400 million will accrue over the course of the MTF's life. He stated that any increase granted should be enough to cover the entire MTF deficit, including the deficit already accrued. He further commented that Chubb had difficulty in understanding how any adequate rate can be determined, even on an interim basis, which does not include IBNR. He further urged that the final rate increase be determined as quickly as possible. (Transcript, pp. 73-79).

As set forth in the "Interim Rate Proposal Procedures for the MTF," and announced at the December 4 meeting (Transcript, p. 79) interested members of the public were provided an additional seven days to submit written comments to the Commissioner on the proposed interim rate increase. This was extended to nine days to accommodate the receipt of late and illegible-as-telecopied comments in light of some commenters' complaints about the brevity of the comment period. Twelve written comments were received representing the views of seven insurance companies, an insurance trade association, a producer trade association, two consumer organizations and the Division of Rate Counsel, Department of the Public Advocate (Public Advocate). The substance of these various comments are discussed further below.

The MTF proposes an interim rate increase of 22 percent on liability coverages (11.2% on bodily injury liability and uninsured/underinsured motorists; 5.4% on property damage liability; and 70.4% on personal injury protection) resulting in a 15 percent overall increase in revenues to the MTF. The proposed interim increase would be effective January 15, 1992.

The OCS Report dated December 3, 1991, which accompanied the application, found the maximum possible range of the MTF's indicated rate level need from plus 15% to plus 50%. It noted that the maximum probable range was from plus 24% to plus 42% with the most probable result at the mid-point of the range, plus 32%, and with the probabilities tapering to 0% at each end of the range. The OCS Report further cautioned that rates less than the probable range would be actuarially unsound and likely to result in a deficit in the MTF.

The OCS Report sets forth certain conditions and limitations on the data and analysis it contains. First, the OCS Report noted that it was prepared on an expedited basis using methodologies which "contained assumptions and limitations which might be more explicitly considered in a more detailed study." These included: calculations assuming the MTF was an on-going operation; no adjustment to provide for collection of the required rate despite an incomplete policy term; no consideration for recoupment of possible past losses; no consideration in the calculation of investment income for the fact that funds may not be available for investment if required to be used to pay prior losses; no evaluation of the effect of the potential changes in the size or mix of the MTF book of business; no adjustment for distortions due to start-up; earned premium at current rates (EPCR) calculated at full value based on the 18.6% rate increase effective June 15, 1991, despite the fact that the amount expected was not realized; start-up costs not explicitly included in the calculation; and IBNR estimated without a detailed study.

Additionally, a review of the filing indicates that a combination of data sources and judgment was relied upon to select trend amounts because of the lack of reliable trend data. Although MTF costs consist primarily of fees paid to the servicing carriers in accordance with contracts, the method of trending expenses was applied in lieu of projecting expenses through calculation by the underlying parameters. In the absence of an IBNR study, the quarterly payout pattern of losses and allocated loss adjustment expenses was adopted from a July 12, 1991 draft financial report, which pattern, the OCS Report stated, appeared to be too short. Investment income was

estimated based upon an interest rate of 5%, although this interest rate is significantly lower than the interest rate normally used by the Department for automobile insurance rate making purposes. (See *N.J.A.C.* 11:3-16.10(c)). No estimate was provided on the effect of cost-saving and cost containment provisions of the FAIR Act although this information was requested. Finally, it must be noted that much of the data used in the filing was originally derived from the operation of the JUA. At the December 4 meeting Neil Pearson, General Manager of the MTF, described the past and continuing efforts to improve MTF operational efficiency by reducing and controlling costs and expenses. (Transcript, pp. 23-39.) One particular program to validate use classification may result in an additional \$10 million in premium. (Transcript, pp. 30-31.)

Of those who submitted written comments on the interim rate increase proposal, the Independent Insurance Agents of New Jersey (IIA), a producer trade association, supported the interim rate increase as proposed, and urged that "any additional rate increase necessary to operate the MTF at a fully adequate, self-funded rate level be implemented as quickly as possible." IAA [sic] also stressed the importance of revising the MTF rate structure to provide auto insurance purchasers with an incentive to seek coverage in the voluntary market. All of the actuarial commenters from both the industry and the Public Advocate addressed the acknowledged limitations of the OCS Report. Their comments and recommendations are set forth below.

The MTF Actuarial Committee, a subcommittee of the MTF Advisory Committee, recommended a 39.4% rate

increase. Although its analysis is not clear, these commenters apparently adjusted the OCS Report's possible range from 15 – 50% to 21 – 58% based upon the following: adjusted for the actual results of the June, 1991 rate increase by adjusting EPCR; adjusted estimated investment income for prior losses; and made higher loss trend selections, although the specific selections were not set forth in the comment. Their recommendation is the apparent mid-point of the possible range.

Selective Insurance Group recommended a 32% interim increase, the mid-point of the OCS Report's possible range. State Farm Insurance Companies commented that the 15% overall rate increase "was not nearly enough," noting that the OCS Report stated that the most probable range was from 24% to 42%, which range it suggested should be adjusted upward by 10% to reflect the following: properly adjusted EPCR; understated investment income; start-up costs; a different, higher trend (not provided) for symbol drift/model year rating which considers the recent decline in new car sales; and another unstated factor that would consider the deteriorating effect of depopulation on the MTF book of business. It recommended a rate increase of at least 32.7%.

Travelers Insurance Companies recommended a 47.2% increase based upon the midpoint of the OCS Report's most probable range (32.7%); correction of EPCR (plus 5.4%); correction of investment income (plus 2.0%); inclusion of FAIR Act savings (minus 1.7%); correction of loss trends (plus 5.6%); correction of expense trends (plus 0.7%). The American Insurance Association recommended an increase within the OCS Report's most credible range of 24 to 42 percent. The Hanover Insurance

Company made no specific recommendations, but provided recommendations and comments that addressed the limitations of the OCS Report. It concluded: "the proposed interim rate level changes is a positive first step yet it . . . falls short of the true rate need."

Allstate Insurance Company asserted that the Department was violating the holding of in *In re: Rate Filing by the MTF* and was acting arbitrarily, capriciously and unreasonably by proposing a two-step process for the adjustment of rates to fund the MTF at the level necessary. Without making a specific recommendation, it stated that the rate increase needed is much higher than the range indicated in the OCS Report, based upon needed adjustments to EPCR, overly optimistic estimates of investment income and other unstated, allegedly faulty assumptions.

Chubb Group of Insurance Companies recommended a 46% increase to be effective January 1, 1992, based upon a study by an actuarial consulting firm which it attached to its comments. It described adjustments to four limitations in the OCS Report: adjustment to investment income; impact of start-up costs; adjustment to EPCR (failure of MTF to realize full effect of previous 18.6% rate increase); and lack of a detailed IBNR study. It stated that its actuarial consultant estimated that the effect of IBNR raises the OCS Report estimated maximum probable range an additional 9%.

From an opposing view, the Public Advocate commented that the 5% interest rate used in the OCS Report's investment income calculation results in investment

income on earned reserves being understated, and suggested the use of an interest rate in excess of 8%. Secondly, the Public Advocate stated that the cash flow patterns employed in the OCS Report also understated expected investment income. Thirdly, the Public Advocate noted the lack of attempt to quantify savings from various FAIR Act reforms; specifically, it urged a 25% reduction in uninsured motorists coverage. It noted that in a recent rate case the Commissioner had found it appropriate to adjust the rate increase granted for anticipated FAIR Act savings. Fourthly, the Public Advocate commented that the loss development factor (including the IBNR factor) should be increased. Fifthly, the Public Advocate commented that from 1988 through 1990, JUA IBNR reserves have been excessive by a total of \$665 million (based upon the JUA Annual Statement) and that IBNR should be a smaller component of the MTF's losses compared to the JUA because of the efforts of the MTF management to reduce costs and expenses. Sixthly, the Public Advocate commented that the procedure used in the OCS Report double counts personal injury protection losses in excess of \$75,000, which are reimbursed by the Unsatisfied Claim and Judgment Fund. New Jersey Citizen Action also commented that the MTF interim rate filing failed to consider provisions of the FAIR Act that will reduce costs. All of these adjustments would serve to reduce the MTF's indicated rate level need, although neither the Public Advocate nor New Jersey Citizen Action recommended a specific figure.

In addition to specific comments on the actuarial data, methodology and assumptions set forth in the OCS

Report, several of the commenters made general comments. The Public Advocate, consumer group commenters and some industry commenters objected to the lack of time to make an adequate review and analysis of the filing. Allstate and other commenters requested access to the data used to develop the filing. New Jersey Common Cause urged that the comment period be extended to 20 days, followed by a public hearing and an additional 3 days for additional written comments as is proposed for inclusion in the MTF Plan of Operation. The Public Advocate noted that the short time for review and analysis was further hampered by the limited data provided in the filing, noting the difference in the data included in the filing from normal personal automobile rate filings, which are accompanied by data set forth in *N.J.A.C.* 11:3-16. Additionally, New Jersey Common Cause urged that no part of an MTF rate increase should be based upon any deficit that is the result of the industry's failure to meet depopulation quotas required by *N.J.S.A.* 17:33-11. It further urged that no increase at all should be granted until April 1, 1992, when MTF insureds have an opportunity to seek coverage in the voluntary market if they are "eligible persons" as provided in *N.J.S.A.* 17:33B-15 and *N.J.A.C.* 11:3-34. New Jersey Citizen Action commented that any MTF rate increase should be denied to the extent that the rate increase is unnecessary to allow insurers to earn a fair rate of return on their business as a whole, considering that the MTF losses would be allocated to MTF member insurers. It further commented that the proposed MTF rate increase should be denied to the extent that it charges policyholders for excessive MTF

expenses, such as commissions and servicing carrier fees that exceed a reasonable level.

As described in Bulletin No. 91-21, the "Interim Rate Proposal Procedures for the MTF" were intended to respond promptly to the decision of the Court in *In re: Rate Filing by MTF*, supra. The Court there did not direct an interim rate increase; rather it directed the Commissioner to meet with interested parties and proceed promptly to establish procedures to set MTF rates at an appropriate level; *N.J.S.A. 17:33B-11c(3)* provides that such procedures are to be part of the MTF Plan of Operation.

Pending the establishment of those procedures as part of the MTF Plan of Operation, and the prompt filing and determination of adequate MTF rates, the MTF has requested an interim rate increase. Generally, personal lines insurance rates are adjusted only after the analysis and review of a detailed rate filing that demonstrates clearly the reasons for the adjustment. See *N.J.S.A. 17:29A-14*. Historically, this has also been true for setting rates in the residual market. For example, JUA rates were those rates used by the rating bureau representing the greatest number of insurers (see *N.J.S.A. 17:30E-13*) and rate changes requiring prior approval of the Commissioner were thus subject to the processes set forth in *N.J.S.A. 17:29A-14*. Since its creation, the Public Advocate's Division of Rate Counsel has participated in the process to protect the public interest. *N.J.S.A. 52:27E-18*. Thus when the process for fixing insurance rates involves public participation, the decision to fix new rates generally awaits the outcome of that process.

The MTF, however, is a transitional facility to which N.J.S.A. 17:29A-14 does not apply. It was created to serve its legislatively mandated purpose for a limited life. Its rates along with all other aspects of its operation are the responsibility of the Commissioner, although no instruction was provided in N.J.S.A. 17:33B-11 about how this responsibility was to be executed except that procedures be set forth in the MTF Plan of Operation. The Court in *In re: Rate Filing by MTF* found that the lack of such procedures was a deficiency immediately to be cured. In doing so, the Court noted that rate increases are prospective only and that past losses from inadequate rates can never be made up. Under the present emergent circumstances, I have determined to provide for an immediate, interim rate increase after opportunity, albeit brief, for interested parties to provide comment, which shall be followed immediately by more studied procedures to fix MTF rates at their proper level in accordance with procedures provided by an amendment to the MTF Plan of Operation.

Although interim rate changes pending the outcome of deliberative processes are generally disfavored, the Commissioner has, however, established interim rates in the past under extraordinary circumstances. Most notably, in *New Jersey State AFL-CIO v. Bryant*, 55 N.J. 171 (1969) the Supreme Court affirmed the Commissioner's decision to approve increased rates for an applicant that was in serious financial distress pending a final determination on its application for permanent new rates. There, in a hearing commenced but not concluded, evidence showed that the applicant had a substantial and

growing deficit; was technically insolvent; and was operating without required minimum reserves. 55 *N.J.* at 174. All parties to the proceedings, including counsel appointed to represent the public interest, acknowledged that some increase was necessary pending a final determination. The interim rate increase was fixed at an amount that could not, in good faith, be disputed by anyone and to which all parties to the proceedings agreed. See 55 *N.J.* at 175.

In the present matter, the interim MTF rate increase application is intended to respond promptly to the Court's directive to undertake immediate action that will ameliorate the accrual of a deficit in the MTF, while also proceeding promptly to fix adequate MTF rates in accordance with proper procedures established in the MTF Plan of Operation. Therefore, I am approving an increase in MTF rates in an amount that approximates the amount requested by the MTF, the low point on the possible range of a permanent increase. In order to accommodate the allocation of the increase as set forth further below, I have been advised that the expected revenue impact is a 14.9% increase. Without question, this amount of increase can be justified regardless of the actuarial assumptions and methodology used, and regardless of what the complete and final data shows when the permanent rate increase filing is made and determined in a more deliberative, analytical and open process.

In approving an interim rate increase for the MTF, I am not unmindful of the issues raised by the comments to the filing. The actuarial commenters raised many excellent points in favor of a higher (and in some cases, a lower) rate adjustment. Commenters requested a better

opportunity to review the data upon which the filing was based. These points should be thoroughly, though expeditiously, explored. Resolution of these issues, however, should occur in connection with the determination of a fully adequate rate for the MTF, not in the context of proceedings to provide an interim rate increase in the present emergent circumstances.

Similarly, I am not unmindful of the comments of those who oppose any MTF rate increase on an interim basis. I recognize that the time to review the filing, and to present comments, has been extremely constrained. Such is the nature of proceedings to fix interim rates. With regard to the comment that no MTF rate increase granted be effective until April 1, 1992, when all eligible persons as defined in N.J.S.A 17:33B-15 may be insured in the voluntary market, I find that such an action would be inconsistent with the directive of the Court in its decision of *In re: Rate Filing by MTF*. Moreover, it would be inconsistent with my own decision, set forth in Order No. A91-212, in which I indicated that I would respond appropriately upon clear indications that MTF rates were deficient.

Finally, I acknowledge the comment that no MTF interim rate increase should be approved that compensates for some insurers' deficiencies to depopulate the residual market as required by N.J.S.A 17:33B-11c(5). Although preliminary figures indicate that this failure may be responsible for as much as \$147 million of the projected MTF deficit, I find that there is no real, good faith dispute that an increase in MTF rates in the amount approved is warranted at this time. All of these issues, as well as those raised by the industry commenters, may be

considered in connection with the permanent increase for which application will soon be made.

With regard to the proposed allocation of the rate increase to liability coverages, however, I find that public policy militates against MTF rates being raised in that fashion. The previous MTF rate increase effective June 15, 1991, increased the rates of only those MTF insureds with at-fault accidents or automobile insurance eligibility points. Persons with neither continued to pay the same rates as were established for the JUA as of October 1, 1990. The previous MTF rate increase fell most heavily on those MTF insureds who were within the second tier of the JUA/MTF rate structure.

At the time the decision was made to allocate the June 15, 1991 rate increase to drivers with at-fault accidents and automobile insurance eligibility points, it appeared that more than half of the drivers insured by the MTF would be subject to the higher rates because of their driving history record. Moreover it appeared likely that drivers with clean records would be the first to be absorbed into the voluntary market, further increasing the proportion of MTF insureds to which the increase would apply. The preliminary information proved not to reflect current conditions, however, and the latest information shows that over 60% of MTF insureds have clean driving records.

In some instances, present MTF rates for drivers without at-fault accidents or automobile insurance eligibility points remain less than for similar drivers in the voluntary market. A residual market mechanism should not routinely provide rates less than those charged to

insureds in the voluntary market. As one commenter specifically noted, maintaining lower rates in the MTF makes its depopulation more difficult as it creates a disincentive for eligible insureds to seek coverage from a voluntary market insurer.

For these reasons, I have determined that rather than approve the increase as proposed (allocated to the liability coverages as set forth in the MTF interim rate filing) the MTF rate increase shall be the same percentage for both the liability and physical damage coverages (excluding personal injury protection, uninsured/underinsured motorists and expense fees) and allocated by auto insurance eligibility point level as set forth in the Appendix to this Decision and Order. I find that this allocation of the increase will better serve the public policy purposes identified above, and, I hope, speed depopulation of the MTF, while providing interim rate relief approximately equal to the amount requested.

In approving this interim rate increase for the MTF, I reiterate my commitment to move expeditiously to provide fully adequate rates in the MTF as promptly as possible. I note that the comment period for the Rate Proposal Procedures for the MTF, proposed as an amendment to the MTF Plan of Operation, has ended. I expect that appropriate procedures will be promptly established in the MTF Plan of Operation, and that a proposal for rate adjustment for the MTF to yield fully adequate rates will be submitted immediately thereafter. This permanent rate proposal will be promptly addressed pursuant to procedures as established.

Now, therefore

IT IS on this 20th day of December, 1991

ORDERED that:

1. The MTF request for an interim rate increase is approved, as modified, in the amount of 14.9 percent;
2. The MTF request for the overall increase to be allocated to all liability coverages, as set forth in its December 4, 1991 filing is disapproved;
3. The approved overall increase shall be allocated to both liability and physical damage coverages and allocated by auto insurance eligibility point level as set forth in the Appendix to this Decision and Order; and
4. The MTF rates as modified in this Decision and Order shall be effective for new and renewal policies on and after January 15, 1992.

This Decision and Order constitutes a final agency decision and is effective immediately. Any appeals from this Decision and Order shall be filed with the Clerk of the Superior Court, Appellate Division, within 45 days of the date hereof, pursuant to the Rules Governing the Courts of the State of New Jersey.

12/20/91

Date

/s/ Samuel F. Fortunato
Samuel F. Fortunato
Commissioner

DB42/ORDERS

APPENDIX

Auto Insurance Eligibility Points	Percent of Risks	Average Old Premium	Average New Premium	Percent Increase
0	61.30%	\$ 763	\$ 986	29.2%
1	1.30	1,011	1,041	3.0
2	7.30	864	1,051	21.6
3	2.50	1,061	1,061	0.0
4	8.20	1,277	1,277	0.0
5	7.10	1,581	1,581	0.0
6	1.50	1,342	1,342	0.0
7	1.40	1,689	1,689	0.0
8	1.30	1,529	1,529	0.0
9	2.00	1,768	1,768	0.0
10	1.30	2,201	2,201	0.0
11	0.80	1,510	1,510	0.0
12	0.80	1,987	1,987	0.0
13	0.40	1,664	1,664	0.0
14	0.80	1,987	1,987	0.0
15	0.40	2,621	2,621	0.0
16+	1.60	2,143	2,143	0.0
<u>TOTALS</u>	<u>100.00%</u>	<u>\$1,010</u>	<u>\$1,161</u>	<u>14.9%</u>

Approximate number of insureds affected by increase:
419,400

Estimated total increase in MTF revenue: \$90.4 million

DB42A/ORDERS

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IN THE MATTER OF)	SUPERIOR COURT OF
THE COMMISSIONER)	NEW JERSEY
OF INSURANCE'S)	APPELLATE DIVISION
DECEMBER 20, 1991	)	DOCKET NO. A-
ORDER REGARDING THE)	
DECEMBER 4, 1991 RATE	)	NOTICE OF APPEAL
FILING BY THE MARKET)	
TRANSITION FACILITY	)	On Appeal from a Final
OF NEW JERSEY	)	Decision and Order of
	)	The Commissioner of the
	)	Department of Insurance

TO: Edward Dauber

Acting Attorney General of the State of New Jersey

By: Joseph L. Yannotti, D.A.G.

Richard J. Hughes Justice Complex, CN-112

Trenton, New Jersey 08625

Attorneys for New Jersey Department of Insurance
and Commissioner of Insurance

Hon. Samuel Fortunato

Commissioner of Insurance

20 W. State Street, CN-325

Trenton, New Jersey 08625-0325

Theresa D. Brown
Department of the Public Advocate
Division of Rate Counsel
31 Clinton Street, 11th Floor
P.O. Box 46005
Newark, NJ 07101
Attorneys for the Public Advocate
The attached Counsel List

PLEASE TAKE NOTICE THAT Allstate Insurance Company ("Allstate"), appeals to the Superior Court of New Jersey, Appellate Division, from an Order of the Commissioner of Insurance (the "Commissioner") dated December 20, 1991, but not received until December 23, 1991, granting the Market Transition Facility ("MTF") of New Jersey a 14.9% interim rate increase, which is a final agency action pursuant to R. 2:2-3. Allstate appeals from this Order for the following reasons:

- (1) The MTF rate Order does not provide for a rate increase sufficient to cover the cost of insuring the MTF population, and is therefore contrary to law; and
- (2) The Commissioner acted arbitrarily and capriciously in issuing an MTF rate Order which grants the MTF only a small portion of the necessary rate relief and which disregards the recommendations of the Commissioner's own actuarial consultants.

A copy of the Order appealed from is attached as Exhibit "A" to the Case Information Statement submitted herewith.

Pet. Supp. App. 24

Smith, Stratton, Wise,
Heher & Brennan
Attorneys for Appellant
Allstate Insurance Company

By: /s/ Penny A. Bennett
Penny A. Bennett

Of Counsel:

Duane C. Quaini
William T. Barker
Steven Levy
Sonnenschein Nath & Rosenthal
8000 Sears Tower
Chicago, Illinois 60606
(312) 876-8000

Princeton, NJ
December 27, 1991

ORDER ON EMERGENT APPLICATION

I/M/O COMMISSIONER OF INSURANCE'S DECEMBER 20, 1991 ORDER REGARDING THE DECEMBER 4, 1991 INTERIM RATE FILING BY THE MARKET TRANSITION FACILITY OF NEW JERSEY	SUPERIOR COURT OF NEW JERSEY APPELLATE DIVISION DOCKET NO. A-2141-91T5 MOTION NO. M-2422-91 BEFORE PART: C JUDGES: PETRELLA COHEN STEIN
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EMERGENT APPLICATION FILED: 12-30-91 BY:
THOMAS HASTINGS, ESQ., MICHAEL R. COLE, ESQ.,
STEVEN M. LEVY, ESQ.

ANSWER(S) FILED: 12-30-91 BY: N.J. ATTORNEY GEN-
ERAL; ELMER M. MATTHEWS, ESQ.
APPEARANCE ONLY: THERESA D. BROWN, ESQ.
DATE ARGUED: 12-30-91

ORDER

(Filed Jan. 8, 1992)

THIS MATTER HAVING BEEN DULY PRESENTED TO
THE COURT, IT IS ON THIS 30TH DAY OF DECEMBER,
1991, HEREBY ORDERED AS FOLLOWS:

EMERGENT	GRANTED	DENIED	OTHER
APPLICATION FOR		X	
EXPEDITE APPEAL			
AND PRELIMINARY			
RELIEF PENDING			
DISPOSITION OF			
APPEAL			

SUPPLEMENTAL:

Allstate and Chubb have appealed the December 4, 1991 interim rate order of the Commissioner of Insurance for the Market Transition Facility. They moved on an emergent basis for an acceleration of the appeal proceedings, and for an interim rate order from this Court requiring the Commissioner to set higher MTF rates pending the appeal.

We deny the application for an interim rate order. We do so out of doubts as to our authority to make such an order, and out of an absence of a record before us to show the quantitative impact on the appellants or the public of the grant or denial of such relief, either as writers of MTF depopulation business at MTF rates or as potential sharers of an MTF deficit.

We also deny the application for acceleration. We do so because the Commissioner is complying with our November 19 mandate, even to the extent of setting interim rates while considering a permanent rate, because the interim rate is likely to be in effect, according to the Commissioner's timetable, for only several weeks, and thus the matter will become moot even as we are

considering it. We base this ruling on representations from the Commissioner about the pace of future proceedings.

FOR THE COURT:

/s/ Richard S. Cohen

RICHARD S. COHEN, J.A.D.

MTF Market Transition Facility of New Jersey
[logo] 293 Eisenhower Parkway,
Livingston, New Jersey 07039
(201) 533-1165

January 24, 1992

Hon. Samuel F. Fortunato
Commissioner of Insurance
NJ Department of Insurance
20 West State Street
CN 325 12th Floor
Trenton, NJ 08625

Re: Market Transition Facility of New Jersey
Final Rate Proposal.

Dear Commissioner Fortunato:

The Market Transition Facility, pursuant to the recommendation of the Advisory Committee, is hereby submitting a rate change proposal. It is intended that this rate change will allow the MTF to operate on a break-even basis prospectively from the date of implementation, i.e. April 1, 1992.

Included in this proposal is the actuarial analysis from the MTF's consulting actuary, O'Neil Consulting Services, that will support the requested overall rate increase of 16.8%. It should be noted, however, that annual premiums will not increase by this percent due to the fact that this increase will only apply to those policies, new and renewal, incepting between April 1, 1992 and September 30, 1992, these dates inclusive.

Finally, it must also be pointed out that as of September 30, 1991, the MTF's share of the State's private passenger

automobile market should have been 25.0%; however, due to the failure of certain voluntary market insurers in meeting their depopulation quotas, the MTF has a share of 31.72%. From the data available, it is not clear whether the MTF's total loss ratio has increased or decreased due to this situation. Therefore, no such effect is utilized in this analysis.

If you have any questions, please do not hesitate to contact me.

Very truly yours,

/s/ R. T. Haskins
R.T. HASKINS, CPCU, CLU
Special Deputy Commissioner

RTH/hm

cc: Jasper Jackson, Deputy Commissioner

FILING MEMORANDUM

New Jersey Market Transition Facility

The New Jersey Market Transition Facility retained the services of O'Neil Consulting Services to develop an estimate of its overall rate level needs. The results of that analysis are summarized in the attached report. It should be noted that the analysis includes a number of limitations as identified in the report.

The purpose of this memorandum is to propose a +16.8% overall rate level change effective April 1, 1992. It should be noted that this is a going-concern rate level effect. The

MTF will realize only about one half of the income associated with this amount because it ceases operations on September 30, 1992.

The proposed +16.8% rate level change would be distributed by coverage as indicated by the rate level calculations. The proposed changes by coverage are shown on the attached Exhibit A. No other distributional changes are proposed.

January 22, 1992

Report on
Rate Level Requirements
for the
New Jersey Market Transition Facility

Prepared for the MTF by:
O'Neil Consulting Services
January 22, 1992

New Jersey Market Transition Facility-
Report of Rate Level Indication Analysis

I. INTRODUCTION

O'Neil Consulting Services was retained by the New Jersey Market Transition Facility (MTF) to estimate its indicated rate level requirements. This report outlines the data, assumptions and methodologies underlying the requested calculation.

This report is an update of a report dated December 3, 1991 which used MTF data thru August, 1991. This study is based on the first full year of MTF experience, using data from the MTF's inception at October 1, 1990 thru September 30, 1991. This report was also prepared in an expedited time frame. However, some of the procedures which were previously modified or adapted from other studies were reviewed and adjusted as necessary. These areas are noted as applicable in this report.

This report is organized into the following sections: background, conditions and limitations, results, data, and assumptions and methodologies.

The underlying data and information included in this study were compiled as required by the DOI according to the Commissioner's latest amendment to the MTF plan of operation setting forth Rate Proposal Procedures. The MTF is specifically excluded from the provisions of N.J.A.C. 11:3-16.1.

II. BACKGROUND

The MTF was created by Section 88 of the FAIR Act and became operational on October 1, 1990. This operational date was coincident with the date after which the JUA (AFIUA) was prohibited by the FAIR Act from issuing or renewing automobile insurance policies. The MTF is a temporary market mechanism designed to facilitate the transition of "eligible" drivers, as defined in the FAIR Act and attending regulations, from the JUA to coverage in the voluntary market. The MTF has only a two year life span. Under the FAIR Act, the MTF was initially authorized to charge the JUA rates. On January 17, 1990, the MTF filed a request for an overall increase in rates with the Commissioner. On May 10, 1991, the Commissioner granted an overall 18.6% premium increase to the MTF, effective June 15, 1991. On December 4, 1991, the MTF filed for an overall 15.0% increase in rates. The Commissioner approved an overall 14.9% rate increase effective January 15, 1992.

III. CONDITIONS AND LIMITATIONS

The analysis herein was based on the data and information provided by the MTF. No independent audit or verification of the data/information was completed. To the extent such data/information was either inaccurate or incomplete, the results derived therefrom will also be inaccurate, incomplete, and/or biased. To the extent possible, areas of such deficiency were identified and discussed. Further, this analysis projects loss and expense costs into a prospective rating period. All such projections are estimates and may err due to various unforeseeable [sic] contingent events. These include, for example, additional law changes, changes in regulation, or changes in policy/claim handling procedures.

Finally, as noted above, certain of the limitations present in the last study were adjusted for this study. However, it was not possible to address all of the limitations previously identified. The remaining limitations are listed below without explanation. Specifics of these limitations are discussed where applicable in this report.

1. All calculations were completed as if the MFT [sic] were an on-going operation. Trend periods, etc. are fully included for both income and outgo.
2. No adjustment was made to provide for the incomplete policy term available for collection of the required rate.
3. All calculations are prospective. No consideration was given to recoupment for possible past losses.

4. No attempt was made to quantify or evaluate potential changes in the size or mix of the MTF book of business.

5. No attempt was made to adjust the data for distortions due to start-up of the MTF such as the lag in earned premium.

Four of the limitations identified in the December 3, 1991 study have been eliminated in this report. They were: adjustment of the 18.6% rate level change to the realized amount, determination of IBNR from a detailed analysis of the required IBNR, adjustment of investment income due to use of cash to fund prior period losses, and disposition of the issue of start-up costs. These are discussed further in the following sections.

IV. RESULTS

The current analysis of the MTF rate level needs resulted in an overall indicated rate level change of 16.8%. Results by coverage are shown on Exhibits 1 and 2.

The effective date underlying the indicated rate level changes is 4/1/92. It should be noted that since the MTF ceases operations on 9/30/92, only about half of the required additional revenue will be realized prior to that time.

V. DATA

The underlying data were taken primarily from monthly summaries of operations provided to the MTF by AIPSO. The data are by policy year and accident year from inception of the MTF, October 1, 1990, thru September 30, 1991,

the first full year of MTF operation. Data elements provided were extensive and included, income items: written premium, earned premium, written DIP/DRDP, earned DIP/DRDP, and outgo items: paid loss, outstanding loss, UCJF recoveries, paid ale, directly reimbursable expenses, SIU expenses, claim service fees, non-claim service fees, and commissions written.

Data were also obtained from a variety of other sources. Administrative costs, premium taxes, and the expected UCJF assessment were estimated from the MTF Financial Statements.

VI. ASSUMPTIONS AND METHODOLOGY

The assumptions and methodology associated with each step of the calculation are described below.

A. Income Items

1. Written Premium

DIP/DRDP written premium was available only for all coverages combined. For purposes of determining the required rate level by coverage, DIP/DRDP written premium was apportioned to all coverages excluding PIP based on the proportion of each coverage's written premium to total written premium. This is a change from the last report wherein DIP/DRDP was allocated to the liability coverages only. This approach was revised because it was noted that the DIP/DRDP factors generate revenue for all coverages except PIP.

2. Earned Premium

Earned premium by coverage was taken from the AIPSO monthly statistical reports as equal to written minus unearned at the end of the period. At the last study, earned premium by coverage was estimated because neither earned nor unearned premium were available by coverage for the non-quarter ending month of that experience period (August). Earned DIP/DRDP was similarly calculated and then allocated to coverage in proportion to earned premium by coverage.

Subsequent to the last study, an overstatement in earned premium was discovered by the MTF in the amount of \$33,144,215. Because the auditors were unable to provide the corrected earned premium by coverage, the error was allocated to coverage in proportion to the uncorrected earned premium by coverage.

3. Earned Premium at Current Rates/Premium Trend

Effective June 15, 1991, the MTF was granted an 18.6% premium increase in the form of the DRDP rating factors and increased flat dollar accident surcharges. Due to time constraints, for the last study, this increase was included at full value despite a dramatic difference between the proportion of clean/surcharged risks underlying the 18.6% and the actual proportion present in the MTF. Therefore, for this study, the 18.6% was reevaluated using the current distribution by DRDP point. This calculation resulted in an estimated realized prior premium increase of 12.3% instead of the 18.6%.

The factors utilized by the DRDP apply to all coverages except PIP while the flat dollar accident surcharges relate to all coverages. Accordingly, the effect of the 12.3% rate level change was apportioned to DRDP and the effect of the increased accident surcharges. This computation resulted in premium effects of 13.5% for all coverages except PIP and 5.1% for PIP. An on-level adjustment factor was developed using the parallelogram method and applied to all coverages. The on-level factors were 1.131 for all coverages except PIP and 1.049 for PIP.

The January 15, 1992 rate level change of 14.9% applied to all coverages except PIP and UM. The effective change by coverage other than PIP, was, therefore, 17.0% based on the distribution of earned premium by coverage. This amount was included in the on-level factors at full value.

Physical damage coverages were also adjusted to provide for model year rating and symbol drift. Due to time constraints at the last review, the factors developed in the Mercer draft report of July 12, 1991 were used. These were, 14.1% for comprehensive and 9.9% for collision. Since the last study, these data were reviewed using the data of a major New Jersey insurer, and found to be appropriate.

Due to start-up of the MTF operation, earned premium is probably somewhat understated relative to a going concern operation. No attempt was made to adjust for this observation.

4. Investment Income

Investment income was incorporated into the permissible loss ratio by applying a cash flow approach to the other income/expense items. This method and its various parameters is described in a later section. It was noted that actual investment earnings to date for the MTF have been only slightly above 2%. It is not clear why the MTF has not achieved a higher yield. However, discussions with the MTF representatives indicate that a higher yield of 5% is expected, given current market yields and the type of investments held by the MTF. The selected yield was, therefore, set at the expected level of 5% in accordance with the DOI Rate Proposal Procedures for the MTF as noted above. (The MTF is not subject to N.J.A.C. 11:3-16.10(a)8.)

At the last study it was observed that the investment income calculation did not anticipate the fact that some funds may not be available for investment if they must be used to pay prior period losses. Given the stated first year MTF deficit of about \$375 million, it was assumed that about 25% of the second year written premium would be required to pay these prior period losses and would not be available for investment. Therefore, the value of investment income was estimated based on 75% of the new written premium.

5. Premium Installment Fees

The total amount of such fees thru September was \$13.9 million according to the MTF preliminary financial statement. This amount was included as an add-on to the otherwise calculated on-level earned premium. It was

distributed to coverage in proportion to written premium.

B. Losses

1. Paid Loss, Outstanding Loss, IBNR

Paid loss was taken from the AIPSO reports for the first twelve months of the MTF operation. As for the last study, PIP was net of UCJF recoveries and comprehensive and collision were net of salvage and subrogation. IBNR was taken from a detailed IBNR study by OCS dated January 11, 1991.

2. Loss Trend

Since the last study, one additional quarter of New Jersey, New York, and Countrywide fast track data have become available. Also three additional months of CPI data have become available. These data and the previous selections were reviewed carefully as discussed below.

Because there have been numerous law changes over the last several years, the available New Jersey trend data often produce meaningless results. Therefore, a combination of data sources and judgment was relied on in selecting trend amounts. The data sources included Fast Track thru September, 1991 for New Jersey, New York (BI only), and Countrywide, various CPI cost indices, and data thru June, 1991 for internal ISO trend data for PD. The selected amounts are described by coverage below.

The internal trend data furnished by ISO for the MTF were thru June, 1991 for voluntary and residual market business combined and for residual market business

alone. These data have two basic inherent difficulties as follows: (1) ISO did not collect data for the AFIUA (residual market) for all carriers until second quarter 1989, (2) one of the servicing carriers (CSC) has not reported claim count information to ISO. The first difficulty distorts trend indications based on more than 5 points (from June, 1990 to June, 1991). Therefore, 5 point indications were calculated and reviewed. The second difficulty was eliminated by ISO's estimate of CSC claim counts. No independent review of these estimates was made. Given the limitations of these data, their resulting indicated trends were used only as a final reference in the selection process.

a. Bodily Injury

Because of the changes in the no-fault threshold over the last seven years, New Jersey BI Fast Track and internal trend data are not meaningful as a reference in selecting trends.

Other potential sources of data include Fast Track data from other states or countrywide and CPI data. Fast Track data from other states or countrywide are not particularly relevant because of different underlying laws, most importantly the no-fault threshold. New York does have the same verbal threshold as New Jersey. However, the New York threshold has been in place since 1978 while the New Jersey threshold has only been in place since 1989 and is optional rather than mandatory. Therefore, the current New York data are not directly applicable to New Jersey and must be reviewed with caution. Countrywide data are even less relevant to New Jersey because of

the mix of underlying laws, traffic patterns, claims consciousness differences, etc.

Nevertheless, all three data bases (NJ, NY, and CW) were reviewed and indicated trends were calculated. As expected, the New Jersey data were distorted displaying large negative pure premium indications. The country-wide data are more stable with frequencies around +2% to +4% and severities at around +6% to +7%. On the other hand, the New York data show low but stable severities at about 3.5% to 4% combined with rapidly increasing frequencies, now in the range of +8% to +10%. These results appear odd with severities well below current CPI indices. Given New York's comparatively low level of PIP benefits, a relatively high proportion of uncompensated medical costs could be expected to be found in the BI coverage. The high frequency changes suggest that the New York threshold has begun to erode. Given the recency of the introduction of the verbal threshold in New Jersey, a similar conclusion here would be unreasonable.

The CPI data indicate that costs are increasing at about 7% per year for services (specifically, 5.7% for Physician's Services and 8.4% for the Medical Care Cost Index) and at about 9% to 10% for hospital costs (specifically, 8.5% and 10.7% for Hospital Rooms and Outpatient Hospital, respectively) the total weighted CPI cost index is 7.6%.

All of the above factors and considerations were synthesized into a BI pure premium trend selection of 7.5%, just slightly above the 7.3% selection derived in the last study. This is consistent with the New York data adjusted to a basis prior to the apparent erosion of the verbal threshold. (For example, CW frequency and NY severity, both at

about +3.5% combine to about a 7% pure premium trend). It is also consistent with the latest CPI cost data and with the value contained in the prior Mercer report prepared for the MTF.

A summary of the indicated and selected trends trends [sic] is shown on Exhibit 4.

Given the number and kinds of law changes that have taken place over the last several years, the ISO trend data were not useful as support for the selected BI trend.

b. Property Damage

For property damage frequencies and severities, New Jersey and Countrywide Fast Track data were relied on. In addition, various CPI indices which relate to automobile repair labor and parts costs were referred to in order to temper and evaluate the reasonableness of the resultant selections.

New Jersey Fast Track data have been showing declining frequency *and* severity trends for the last two years, particularly the last year. There has been speculation that although there have been no direct coverage amendments to PD, that the changes in other coverages and other reforms, such as the surcharge plan, have caused these declines rather than a "real" decline in accidents or costs. Countrywide fast track data, however, mirror the changes observed in New Jersey, albeit, somewhat lagging behind the New Jersey experience. These data, therefore, confirm the validity of indications based on the New Jersey data.

Fast track frequency trends have been dropping for the last four years. Specifically, CW indicated frequency trends thru September, 1991 were -1.5%, -1.9%, -2.9%, and

-4.9% for the last 19, 12, 9, and 6 points, respectively. New Jersey indicated frequency trends for the same periods were -5.0%, -6.3%, -7.5%, and -7.0%, respectively. The current New Jersey data indicate a possible leveling of the rate of decline recently experienced. The internal data show similar, but somewhat higher indicated frequency trends, at around the -5.0% to -2.0% level, with a slowing in the rate of decline (as suggested by the Fast Track data). Because of the distortions in these data, however, they were given less credibility than the Fast Track data. Therefore, the -5.0% frequency trend selection made for the last study was retained.

Indicated severity trends for New Jersey have also shown a declining [sic] pattern. Fast track indications thru 9/91 for 19, 12, 9 and 6 points were 8.6%, 4.9%, 2.3%, and 0.8%, respectively. Countrywide indications for the same time periods were 6.7%, 4.8%, 3.8%, and 2.5%, respectively. Again, countrywide indications have been moving in the same direction as the New Jersey indications, but at a somewhat slower pace. The internal trend indications were also at about 3%. The most recent CPI cost data averaged 3.6% while the ADP parts indices averaged -1% (although this was skewed by the somewhat old -3% ADP salvage index). These various indications suggest a prospective average claim cost of about 2% to 3%. Such a selection, coupled with the selected frequency change, would result in a negative pure premium trend for this coverage. Although this would be supported by the most recent New Jersey and countrywide data, this was considered to be too speculative a choice at this time. Therefore, the 7% severity trend selected for the last study was retained. This results in a pure premium trend of 1.7%, which is consistent with a combination of the New Jersey

and countrywide 12 point pure premium indications, the latest internal trend indications, and the weighted CPI indices.

A summary of the indicated and selected frequency and severity trends is shown on Exhibit 4 pages 1 and 2.

c. Personal Injury Protection

Coverage changes in the form of higher deductibles and co-payment requirements have caused distortion in the observed PIP trend data. For this coverage other relevant surrogate data were not readily available. Until the FAIR Act, New Jersey was one of only two states to include unlimited medical expense benefits in PIP. At the same time, the New Jersey wage loss benefits at the base of \$100 per week were rather low. The combined PIP package, however, initially provided on a first dollar basis, was richer than any other state. Therefore, the observed severity trends from other jurisdictions are not comparable nor relevant to New Jersey. Therefore, cost information may only be obtained by reference to the various medical cost indices (since more than 90% of PIP losses are due to medical expenses). As noted above the average of these indices is currently at 7.6%.

Frequency trends from other jurisdictions have limited relevance due to the mix of underlying laws, traffic patterns, etc. However, they may be used as a reference point in reviewing PIP frequency trends. The observed countrywide frequencies have been stable for the past year at about 2.5%.

Given these data, a pure premium trend of 9% was selected. This was adjusted by 1% to 8% in consideration

of the FAIR Act's introduction of the medical fee schedule. This selection is consistent with the 7.9% selected for the last study.

A summary of the indicated and selected frequency and severity trends is shown on Exhibit 4.

Given the number and kinds of law changes that have taken place over the last several years, the ISO trend data were not useful as support for the selected PIP trend.

d. Comprehensive

Indicated trends based on New Jersey Fast Track data suffer from distortion due to shifts in distribution of business by deductible. However, current values show declining trends similar to those observed for PD. Although not directly comparable, a similar downward pattern appears in the countrywide Fast Track data.

Given that no valid data for this coverage were available, an 8% change in pure premium was judgmentally selected. This is consistent with the last available ISO trend calculated excluding wind and water losses at 8%. This is 2 points higher than the 6% selected at the last study which gave greater recognition to the current CPI indices. Given the possible volatile nature of this coverage, this position was reconsidered and the full 8% included herein.

e. Collision

Because these data were also distorted due to shifts in distribution of business to higher deductibles, the pure premium trend for this coverage was set equal to the PD pure premium trend at 1.7%. This is consistent with the various

CPI cost indices. A summary of the indicated and selected frequency and severity trends is shown on Exhibit 4.

f. Trend Period and Method of Application

The selected frequencies, severities, or pure premiums, as applicable by coverage, were trended exponentially. The trend period was from the average date of loss in the historical experience period to the average date of loss in the ensuing experience period.

C. Expenses

1. Claim Service Fees Paid

Claim service related costs include the servicing carrier fees, directly reimbursable expenses and the SIU allowance. Servicing carrier fees were treated as unallocated loss adjustment expenses (ule) and subjected to the expense trend procedure. The remaining expenses were treated as ale and included with losses.

The fixed monthly fee paid to Computer Sciences Corporation was allocated to coverage in proportion to the other expenses by coverage.

The last study included these expenses at their paid values. This study reflects the selected ultimate incurred values for DRE and claim service fees developed in the January 11, 1992 OCS reserve study.

2. Non-Claim Service Fees and Other Expenses

Non-Claim service fees were allocated to coverage in proportion to written premium by coverage. A 1% loading, based on observed actual costs to date, was included to cover MTF administrative costs.

3. Expense Trend

MTF costs consist primarily of fees paid to the servicing carriers for policy and claims processing. These fees are based on numbers of policies and numbers of claims. The servicing carrier contracts provide for CPI adjustments to the per unit costs. Therefore, the expense trend procedure based on the CPI parallels this agreement.

The expense trending method consists of developing a current cost factor utilizing the latest CPI indices and trending from that point to the appropriate date in the prospective experience period. For non-claim expenses this is six months beyond the expected effective date of the new rates and for claim expenses it is the expected date of loss in the prospective rating period.

The resultant current cost factor and expense trend values were 1.014 and +3.5%, respectively.

4. Other Expenses

Other expenses include commissions, premium tax, UCJF assessment, start-up costs, administrative costs of operation, and various miscellaneous expenses. The following assumptions were made regarding each expense item.

a. Commissions

These were set at the ratio of actual commissions written to premiums written as provided on the AIPSO reports. This resulted in the unexpected amounts of 8.2% for liability and 9.2% for physical damage.

b. Premium Tax

This was derived from the figures included in the MTF financial statements at 0.25%.

c. UCJF

The MTF has set aside provision for a 7.7% UCJF assessment. Note that this is the anticipated 1992 assessment level based on information from the MTF. This factor represents an increase over the 7.3% included in the last study based on the UCJF 1991 assessment level.

d. Start-Up Costs

MTF servicing carriers were reimbursed for start-up costs in the amount of \$5.6 million. Because this was a one time cost, it is not an amount which should to [sic] be built into the permanent future rate structure. Therefore, it was not included in the calculated required rate level derived herein. However, it is an amount which the MTF must fund at some point, and now is part of the MTF deficit.

e. Administrative Costs

According to its financial statement, the MTF has current operating costs of about 0.7%. This was increased to 1% based on information from MTF management.

f. Miscellaneous Expenses

The MTF financial statement displayed various miscellaneous expenses which are not all captured within the MTF administrative allowance. These include items such as premiums charged off. There are also offsetting items such as commissions charged off. For expediency these items were not explicitly relected [sic] in these calculations. Their effect on the overall result would be minimal.

D. Cash Flow Analysis

The various income and outgo items were included at the values cited above. The timing of each item is described below. As noted earlier, a 5% discount factor was applied.

1. Premium Collection

The quarterly collection pattern of 58%, 14%, 28%, and 28% was based on the MTF six pay plan. As noted above, these values were adjusted by a factor of 75% for purposes of calculating the expected value of investment income.

2. Loss and ALE

The quarterly payout patterns were taken from the January 11, 1992 OCS reserve study. These patterns reflect expected closure of all claims within a ten year period for BI and PIP and shorter periods for the property coverages.

3. Commissions

Commissions were expected to be paid within the first quarter.

4. Premium Tax

Premium tax was estimated to be paid in the second quarter.

5. UCJF Assessment

This assessment was expected to be paid in the fifth quarter.

6. General Expenses (Non-Claim)

These expenses were expected to be paid equally in the first four quarters.

7. Claim Expenses (Unallocated)

These were expected to be paid half over the first four quarters and then in proportion to loss payments.

E. FAIR Act

The FAIR Act contains several provisions which the Legislature intended to result in cost savings. The major provisions through which cost savings may be realized include the following:

1. A medical fee schedule promulgated by the Commissioner and intended to set a cap on costs which impact most directly on the PIP coverage.
2. A requirement that every insurer institute and enforce more detailed anti-fraud plans.

3. Towing and storage fee schedules intended to cap costs connected with physical damage coverages.
4. The requirement that insurers adjust prices for the physical damage coverages in relationship to a driver's provision of anti-theft devices.
5. The requirement for photo inspection of vehicles intended to reduce the cost of physical damage coverages.
6. An amnesty campaign for uninsured motorists.

In reviewing these cost savings opportunities it must be remembered that they became operative at various points during 1991. Therefore to some extent, the historical experience period herein, already reflects some of these savings so that any annualized estimates must be correspondingly adjusted.

Brief review of each of these measures resulted in the following savings estimates by coverage.

1. For BI and PD the FAIR Act provided no cost savings measures.
2. For UM, the amnesty program was largely unsuccessful, with only 11,000 drivers taking advantage of the plan. Further, the DMV penalty procedure is not yet in place. An expected date for operation was not available. The NJ DOI (not OCS) had originally estimated that this program would result in a 25% cost savings for this coverage. Given the remaining short life of the MTF, little to no effect of this program can be expected. Therefore, a 5% savings was reflected in the UM indicated rate level need. The selected 5% factor was based on judgment.
3. For PIP, the medical fee schedule was estimated to save 1% in future costs, and 1% in

historical costs to the extent that they reflected costs incurred prior to the medical fee schedule. Therefore, the trend factor was reduced by 1%. The rate level effect, however, should be nearly fully realized within the historical experience period since the related rules were adopted by the Insurance Department on an emergency basis on November 26, 1990 and on a final basis on January 25, 1991. Nonetheless, the 1% savings was applied to the otherwise estimated required PIP rate level change.

4. For Comprehensive and Collision, the photo inspection program was estimated to produce a savings of 5% based on the results of a similar program in New York. The anti-fraud program was estimated to produce a savings of less than 1%. Thus, 5% was used in total as the estimated savings for these two programs. These plans were effective July 1, 1991, and therefore, were only minimally reflected in the observed historical data.

Therefore, when taken at full face value, the FAIR Act savings were included at an overall rate level effect of -2.1%. However, this may somewhat overstate the value of these reforms to the MTF given the effective dates of the various reforms and the historical experience period relied on for calculations herein.

MTF Market Transition Facility of New Jersey
[logo]

293 Eisenhower Parkway,
Livingston, New Jersey 07039
(201) 533-1165

January 14, 1992

Hon. Samuel F. Fortunato
Commissioner of Insurance
NJ Department of Insurance
CN 325 12th Floor
Trenton, NJ 08625

RE: Report on Fiscal Year Results

Dear Commissioner Fortunato:

Pursuant to Department of Insurance Order No. A91-212, the Market Transition Facility of New Jersey is hereby submitting the financial results of its first fiscal year of operation.

The period covered by this report is October 1, 1990 through September 30, 1991. The results include data on premiums, losses, and operational expenses as well as investment income. The results also include the incurred but not reported (IBNR) loss figure for this period.

The overall deficit has increased from the preliminary estimate of \$300 million to \$375 million for several reasons. Arthur Andersen has confirmed that AMGRO has overstated earned premiums by \$33 million. Another factor was that September developed lower premiums and higher losses than anticipated. The remainder is due to higher IBNR figures.

Our report will be provided to all of the MTF Member Companies.

Very truly yours,

/s/ R. T. Haskins
R.T. HASKINS, CPCU, CLU
Special Deputy Commissioner
RTH/hm

cc: Jasper Jackson, Deputy Commissioner
Neil W. Pearson, General Manager
Henry Witmer, MTF
Member Companies

Date:
14-Jan-92

MARKET TRANSITION FACILITY
BALANCE SHEET
SEPTEMBER 30, 1991

ASSETS:

SHORT TERM INVESTMENTS	\$555,855,461
PREMIUMS RECEIVABLE	347,928,589
RECOVERABLES:	
UCJF RECOVERABLE	1,258,622
NJAI RECOVERABLE	<u>115,625</u>
	1,325,247
DUE FROM NJAFIOA	8,785,545
ACCRUED INTEREST	316,044
OTHER ASSETS	<u>1,101,592</u>
TOTAL ASSETS	<u><u>\$ 915,372,478</u></u>

LIABILITIES AND DEFICIT:

OUTSTANDING LOSSES AND LOSS EXPENSES:

LOSS RESERVES	
(NET OF UCJF OF \$4,372,520)	\$228,561,819
IBNR LOSS RESERVES	254,489,402
DIRECTLY REIMBURSABLE	
CLAIM EXPENSE RESERVE	<u>33,805,000</u>
	516,836,221

UNEARNED PREMIUMS
(INCLUDING DIP AND
DRDP SURCHARGES)

648,844,899

ACCOUNTS PAYABLE AND ACCRUED EXPENSES:

CASH OVERDRAFT	23,804,953
UCJF ASSESSMENT	47,893,489
SERVICING CARRIER FEES - CLAIMS	20,843,009
SERVICING CARRIER	
FEES - OPERATING	13,979,821
BALANCE PAYABLE - NJAIRE	8,731,469
ACCRUED EXPENSES	<u>1,174,255</u>
	117,226,976

OTHER LIABILITIES:

COMMISSIONS	5,651,130
PREMIUM TAX PAYABLE	<u>1,888,834</u>
	7,539,964

ACCUMULATED DEFICIT (374,875,582)

TOTAL LIABILITIES
AND ACCUMULATED DEFICIT \$915,372,478

Date:
14-Jan-92

MARKET TRANSITION FACILITY
STATEMENT OF OPERATIONS
FOR THE YEAR ENDED SEPTEMBER 30, 1991

PREMIUMS (NET OF PREMIUMS RESERVE OF \$850,919,299)	<u>\$669,585,157</u>
LOSSES INCURRED	701,203,919
LOSS EXPENSES INCURRED	107,956,294
COMMISSIONS	112,323,596
OTHER UNDERWRITING EXPENSES:	
PREMIUM TAXES	3,497,440
SERVICING CARRIER FEE	63,585,254
GENERAL AND ADMINISTRATIVE	12,387,477
OTHER ADMINISTRATIVE EXPENSES	<u>85,057,559</u>
	154,507,730
NET UNDERWRITING LOSS	(406,431,382)
PREMIUM CHARGE OFFS FOR UNCOLLECTIBLE PREMIUMS	(2,101,570)
INCOME ATTRIBUTABLE TO FULLY EARNED COMMISSION	5,215,754
INSTALLMENT FEES INCOME	13,943,142
NET INVESTMENT INCOME	<u>14,498,474</u>
OPERATING LOSS	<u><u>(\$374,875,582)</u></u>

[LOGO]

**State of New Jersey
DEPARTMENT OF INSURANCE**

**SAMUEL F. FORTUNATO
COMMISSIONER**

**CN 325
TRENTON, N.J. 08625-0325**

TO: Member Insurers of the Market Transition Facility
FROM: Samuel F. Fortunato, Commissioner
DATE: January 14, 1992
RE: Proposed Amendments to the Plan of Operation of the Market Transition Facility

Enclosed for your information is a proposed amendment to the Plan of Operation of the Market Transition Facility (MTF).

Article V(4) of the MTF Plan of Operation requires a plan to be developed and approved by the Commissioner for the apportionment of the profits or losses among the member insurers.

Article XIV, proposed as an amendment to the Plan of Operation, establishes for use by the MTF a modified (Lloyd's) accounting system using a three-year reporting period. The results of each reporting year will be re-evaluated annually during the three-year cycle. Under the terms of the proposed amendment, there will be no cash call until the completion of the Lloyd's cycle.

Also enclosed is a memorandum advising of the Department's request to the United States Internal Revenue Service for a ruling as to the tax status of the MTF.

Lastly, Article XIV also sets forth the formula for apportioning the MTF operating results among member insurers. If applicable, enclosed is your company's apportionment share of the MTF operating results for the first reporting year. Please be advised that your apportionment share does not include exposure credits earned under the Producer Voluntary Placement Plan (Plan). Member insurers will be contacted shortly about a further opportunity to appoint producers under the Plan whose exposures will be credited towards the April 1991 and October 1991 quotas.

January 14, 1992

Date

/s/

Samuel F. Fortunato
Commissioner

MARKET TRANSITION FACILITY OF NEW JERSEY

PLAN OF OPERATION

ARTICLES OF ASSOCIATION

ARTICLE V

FINANCIAL

1. For the purposes of reporting operating results to member insurers the MTF has adopted a modified "Lloyd's" accounting cycle as set out in Article XIV below. The MTF's fiscal year shall be the calendar year except for the first year of operation which shall be the fifteen month period beginning October 1, 1990.

2. The MTF shall derive its revenue from the following sources for the payment of expenses, losses, loss adjustment expenses, and the provision of adequate,

actuarially sound reserves for unpaid losses and loss adjustment expenses, including incurred but not reported losses in connection with MTF business: (1) net premiums earned; (2) income generated from any MTF violation or accident surcharge system permitted or required by law; (3) income from investment of moneys collected; and (4) assessments from member companies.

3. Any insurer which has ceased to transact automobile insurance in this State shall nevertheless remain liable for revenue due the MTF, as provided in the Plan of Operation.

4. The losses or profits of the MTF shall be apportioned among the member companies as provided by a plan approved by the Commissioner and incorporated as Article XIV of these Articles and may include assessments of member companies or refunds to member companies.

5. The MTF may, from time to time, establish such banking arrangements as may be necessary to further the purposes of the MTF.

Adopted 4/29/91.

ARTICLE XIV

APPORTIONMENT OF MTF PROFITS AND LOSSES

1. For the purpose of reporting operating results to member insurers, the MTF has adopted a modified "Lloyd's" accounting cycle for a three year period with annual reporting. The reporting period is each twelve month period extended from October 1, through September 30.

2. The results of each reporting year described in paragraph 1 above will be reported within 90 days of the end of that reporting year on an interim basis. The results for each reporting year will be re-evaluated annually during the three year cycle. The Member Company's respective shares in the MTF's results will be calculated as described below for each reporting year. No cash call shall be made on Member Companies nor cash profits distributed until the completion of the Lloyd's cycle.

3. A Member Company of the MTF shall be a Member Insurer as defined in Article IV of these articles of Association but shall include a group of two or more insurers licensed to write automobile insurance in this State under common management and control. The Operating Results of the MTF will be apportioned on a group basis.

a. Non-Quota Member Company shall mean a Member Company or group that does not have an individual apportionment share for depopulation because the company entered the market after September 30, 1988.

4. For each reporting year, a determination shall be made whether any Member Company had a Shortfall in Exposures. A Shortfall in Exposures shall be calculated as follows:

a. For the first reporting year, if the average of the in-force exposures of each Member Company of the MTF as reported on September 30, 1990, December 31, 1990, March 31, 1991, June 30, 1991 and September 30, 1991 is less than the average of the Voluntary Market Quotas for that Member Company, as defined in Part I of the Plan of Operation, for the three quota periods ending

September 30, 1990, March 31, 1991 and September 30, 1991;

b. For the second reporting year, if the average of the inforce exposures of each Member Company of the MTF as reported December 31, 1991, March 31, 1992, and June 30, 1992 and September 30, 1992 is less than the average of the Voluntary Market Quotas for that Member Company, as defined in Part I of the Plan of Operation, for the two quota periods ending March 31, 1992 and September 30, 1992;

c. For the third reporting year, if the average of the in-force exposures of each Member Company as reported on December 31, 1992 and March 31, 1993 is less than the Voluntary Market Quota for that Member Company, as defined in Part I of the Plan of Operation, established for the quota period that ends on March 31, 1993.

5. The in-force exposures of the Member Companies shall include exposure credits earned by participation in the Producer Voluntary Market Placement Plan (PVPP).

6. The average in-force exposures for all Member Companies shall be calculated as follows:

a. For the first reporting year, the average of the in-force exposures of each Member Company of the MTF as reported on September 30, 1990, December 31, 1990, March 31, 1991, June 30, 1991 and September 30, 1991;

b. For the second and third reporting years, the average of the in-force exposures of each Member Company of the MTF as reported on December 31, March 31, June 30 and September 30.

7. If there is no Shortfall in Exposures as calculated in paragraph 4 above for the reporting year the net operating results of the MTF, whether a profit or a loss, shall be apportioned among the Member Companies as follows:

a. For Non-quota member Companies, the ratio of the average in-force exposures of the Non-quota Member Company to the average in-force exposures of all the Member Companies for each reporting year as described in paragraph 6 above, shall be multiplied times the MTF profit or loss;

b. All other Member Companies shall have their apportionment share calculated by multiplying the profit or deficit of the MTF, adjusted for that part of the profit or loss apportioned to the Non-Quota Member Companies, by each Company's quota share percentage as determined in Part I of the Plan of Operation, Depopulation of Residual Market, Appendix I, Determination of Member Company Quotas.

8. If there is a Shortfall in Exposures as calculated in paragraph 4 above for the reporting year and the net operating results of the MTF show a loss, a portion of the loss attributable to the failure of Member Companies to depopulate the MTF shall be determined. This portion of the loss and remainder of the MTF loss shall be apportioned among the Member Companies pursuant to paragraphs 9 through 12 below.

9. The portion of the MTF loss that is due to the Shortfall in Exposures shall be calculated as follows:

a. The MTF loss shall be divided by the average of the total exposures in force in the MTF for the reporting year as described in paragraph 6 above. The result is the Actual MTF loss per Exposure;

b. The Actual MTF loss per Exposure as calculated in (a) above shall be multiplied by the total of the Shortfalls of all Member Companies.

10. The Adjusted MTF loss shall be calculated by subtracting that portion of the loss attributable to the failure to depopulate as calculated in paragraph 9 above from the MTF loss.

11. The Adjusted MTF loss shall be apportioned among the Member Companies as follows:

a. For Non-quota Member Companies, the ratio of the average in-force exposures of the Non-quota Member Company to the average in-force exposures of all the Member Companies for each reporting year as described in paragraph 6 above shall be multiplied times the Adjusted MTF loss;

b. All other Member Companies shall have their apportionment shares calculated by multiplying the Adjusted MTF loss, less that part of the loss apportioned to the Non-quota Member Companies, by each Company's quota share percentage as determined in Part I of the Plan of Operation, Depopulation of Residual Market, Appendix I, Determination of Member Company Quotas.

12. Member Companies with a Shortfall in Exposures shall have their apportionment share of the MTF

loss increased because of their failure to meet the statutory obligation to depopulate the residual market. The amount of the increase shall be calculated as follows:

a. The ratio of the Member Company Shortfall in Exposures to the total of all Member Company Shortfalls for that reporting year shall be multiplied by the amount of the MTF loss attributed to the failure of Member Companies to depopulate the MTF.

13. In the event that the MTF results show a loss and a cash call for a Member Company's apportionment share as calculated in paragraph 7 or 11 above is made, the assessment may be permitted as a company expense for the purposes of rate-making:

a. Where the apportionment shares as calculated in paragraph 7 or 11 above would put a Member Company in unsafe or unsound financial condition, the Company may apply to the Commissioner for a deferral or exemption from the assessment.

14. Those companies that failed to meet their depopulation quotas and who receive an additional assessment as described in paragraph 12 above may not include that additional assessment in any rate filing.

15. If there is a Shortfall in Exposures for the reporting year and the net operating results of the MTF show a profit, an amount shall be calculated that represents unrealized profit that would have been made by the MTF had there been no Member Company Shortfalls. That amount shall be deducted from the apportionment of the profit of the Member Companies that had a Shortfall in Exposures.

The profit shall be apportioned among the Member Companies pursuant to paragraph 16 through 19 below.

16. The amount of unrealized MTF profit that is due to the Shortfall in Exposures shall be calculated as follows:

a. The profit of the MTF shall be divided by the average of the total exposures in force in the MTF for the reporting year as described in paragraph 6 above. The result is the Actual MTF profit per Exposure;

b. The Actual MTF profit per Exposure as calculated in (a) above shall be multiplied by a total of the Shortfalls of all Member Companies.

17. The Adjusted MTF profit shall be calculated by adding the unrealized profit as calculated in paragraph 16 above to the MTF profit.

18. The Adjusted MTF profit shall be apportioned among the Member Companies as follows:

a. For Non-quota Member Companies, the ratio of the average in-force exposures of the Non-quota Member Company to the average in-force exposures of all the Member Companies for each reporting year as described in paragraph 6 above, shall be multiplied times the Adjusted MTF profit;

b. All other Member Companies shall have their apportionment shares calculated by multiplying the Adjusted MTF profit by each Company's quota share percentage as determined in Part I of the Plan of Operation, Depopulation of Residual Market, Appendix I, Determination of Member Company Quotas.

19. Member Companies with a Shortfall shall have their apportionment share of the MTF profit decreased because of their failure to meet the statutory obligation to depopulate the residual market. The amount of the decrease shall be calculated as follows:

a. The ratio of the Member Company Shortfall in Exposures to the total of all Member Company Shortfalls for that reporting year shall be multiplied by the amount of the unrealized MTF profit.

20. For purpose of illustration only, assume that at the end of the first accounting year the MTF shows a ~~net~~ loss of \$100 million and there are Member Companies that had an Exposure Shortfall. Assume further that the average total exposures in the MTF equals 1 million and the total of all the Member Company Shortfalls is 200,000. Company A's quota share percentage is 10 percent and its Exposure Shortfall is 30,000 exposures and Company B's quota share percentage is 5 percent and it had no shortfall:

a. The MTF loss per exposure equals \$100. The loss per exposure times the Total Member Company Shortfall of 200,000 equals \$20 million. Therefore, \$20 million of the MTF's total loss of \$100 million can be attributed to the failure of Member Companies to meet their quotas;

b. The Adjusted loss of the MTF is \$80 million. Company A's share of the adjusted loss is \$8 million, 10 percent of \$80 million. Company B's share is \$4 million, 5 percent of \$80 million;

c. Company A, in addition to its apportionment share of the adjusted deficit also receives an additional assessment because it had a Member Company Shortfall in Exposures. The additional assessment is calculated by taking the ratio of Company A's Member Company Shortfall to the total Member Company Shortfall of 30,000/200,000. The result, .15, is multiplied by \$20 million, that portion of the MTF's loss resulting from the failure to depopulate. Company A, therefore, must pay an additional amount of \$3 million in addition to its apportionment share.

[LOGO]

NEW JERSEY DEPARTMENT OF INSURANCE

Samuel F. Fortunato
Commissioner

FOR RELEASE:
January 15, 1992

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(609) 633-3955

INSURANCE DEPARTMENT TELLS COMPANIES THEY
OWE \$180 MILLION FOR FAILING TO DEPOPULATE
MTF; OTHER FINANCIAL DATA SUPPLIED TO COM-
PANIES; NO CASE CALL - IF NECESSARY AT ALL -
UNTIL 1994

TRENTON - The New Jersey Department of Insurance has notified certain insurers that they will bear a \$180 million share of the Market Transition Facility deficit for failing to depopulate the state-run insurer in a timely manner, Commissioner Samuel F. Fortunato announced today.

The Fair Automobile Insurance Reform Law gives the Commissioner the authority to assign a share of the MTF deficit to only those companies that have consistently failed to meet their depopulation quotas.

"The Attorney General gave us a go-ahead to allocate an additional share of the MTF deficit to those companies that have been dragging their feet and not complying with the law," the Commissioner said.

"This part of the deficit should not be spread over the entire industry. It would not be fair to those companies that have opened up the auto insurance market by

working hard to write thousands of new policies every month," Fortunato added.

Fortunato said Allstate bears the largest burden with a \$30.8 million depopulation adjustment allocation. Allstate's total allocation of the MTF deficit is \$64.7 million.

The Commissioner said several major companies have expressed support for the depopulation adjustment allocation.

One company, the Hartford Insurance Group, sent a letter last week to the Commissioner from vice president Henry Katz. Katz said: "While you have not yet asked for input on a plan for sharing of the MTF operating results, we would like to take this opportunity to express our opinion . . . "

"We feel that the MTF operational results participation formula must address the actual performance of companies against their depopulation quotas . . . Failure to include some adjustment to the participation formula to reflect a company's depopulation performance actually rewards companies with quota shortfalls and offers an incentive to avoid writing future quotas," Katz said.

The depopulation adjustment allocations were released as part of a package of MTF financial data supplied to all MTF member companies. Attached is a list of the top 10 automobile insurance writers in New Jersey with their allocation numbers.

The Commissioner said that by failing to take their fair share of MTF drivers, certain companies are also dodging the payment of their fair share of surtaxes and

assessments, which are calculated based on each company's premium volume and were established under the FAIR Law.

The industry is required to pay off over seven years \$1.4 billion of the Joint Underwriting Association's \$3 billion-plus deficit.

The FAIR Law abolished the JUA and created the MTF in order to move drivers out of the state high risk pool and into the private market. To date, nearly 1 million drivers have been successfully moved into the private market.

The \$180 million in depopulation adjustment allocations represents roughly half of the revised MTF deficit figure of \$375 million that was also reported to member companies.

"The deficit would have been much less had those companies depopulated in a timely manner," the Commissioner noted.

Fortunato said the deficit increased after actuaries calculated figures for the MTF's "incurred but not reported" losses. IBNR represents reserves an insurance company needs on hand to pay claims which have not yet been reported.

"The MTF has plenty of cash to continue to pay claims," Fortunato said. "However, we must remain vigilant to keep the MTF financially healthy."

The Commissioner said a significant reason the deficit increased was due to a \$33 million over-reporting of premium by Amgro, one of the three companies writing policies for the MTF.

The Commissioner explained that under a new accounting system adopted by the MTF, the Department will make no cash call, if necessary at all, on any company for its share of the MTF deficit until 1994 at the earliest.

The new accounting system, used for decades by Lloyd's of London, enables regulators to assess the MTF's financial condition for any particular year over a three-year cycle instead of a 12-month period, Fortunato said.

"This system will provide a highly accurate gauge of the MTF's financial condition and whether an industry assessment for any year's operation is finally necessary," he said.

The new accounting system, a hybrid between standard statutory accounting principles and Lloyd's of London syndicate accounting, was developed by Arthur Andersen & Co.

Fortunato explained that the MTF is like no other insurance company doing business in the state. Because MTF's book of business will swell and ebb in a very short period of time, a three-year accounting plan is more practical to use.

"Over a 36-month period, we expect the MTF to go from zero policies to 1.1 million policies then back down to zero," Fortunato continued.

The three-year accounting system allows the Department to evaluate the MTF after each year and notify each member company of the MTF's profits or losses.

Under the former system, if MTF claims outstripped revenues, the Department would be required each to bill the companies for their share of the possible deficit.

Those companies might then apply for a rate increase claiming they could not make an adequate rate of return.

Under the three-year accounting plan, the Department will evaluate the MTF each year and then notify each company of the MTF's financial condition. The financial picture will be adjusted over the next two years and bills will be sent out only if a deficit remains after the end of the three-year period.

"This gives us and the industry a much more accurate insight into the MTF's finances despite a very volatile book of business. Additionally, since the companies do not part with any money until they are billed, investment earnings and income tax savings can be passed on to the New Jersey policyholders," Fortunato said.

The MTF began operation on Oct. 1, 1990 and will issue its' [sic] last policy in Sept. 30, 1992.

* * *

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Market Transition Facility Allocation
of First Year Loss to Top 10 Member Companies

Member Company	Regular Member Co. Allocation	Adjusted MTF Depopulation Allocation	Total Allocation
Allstate	\$33,895,132	\$30,896,312	\$64,791,444
State Farm	23,073,046	0	23,073,046
Prudential	20,371,649	10,942,677	31,314,326
NJ Manufac- turers	18,357,546	0	18,357,546
Liberty			
Mutual	12,540,368	21,157,743	33,698,111
Selective	7,703,556	0	7,703,556
USAA	5,193,257	1,333,300	6,526,557
Ohio			
Casualty	3,729,875	0	3,729,875
Keystone	3,351,551	748,863	4,100,414
Aetna	6,114,854	13,584,668	19,699,522

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[SECOND REPRINT]

SENATE, NO. 3577

STATE OF NEW JERSEY

INTRODUCED JUNE 17, 1991

By Senators FOY, CARDINALE,
O'CONNOR, DiFRANCESCO,
RICE, BUBBA and CONTILLO

AN ACT concerning certain producers of record and
amending P.L.1983, c.65 and P.L.1990, c.8.

BE IT ENACTED *by the Senate and General Assembly of
the State of New Jersey:*

1. Section 28 of P.L. 1983, c.65 (C.17:30E-14) is
amended to read as follows:

28. a. Within 45 days of the effective date of [this
1988 amendatory and supplementary act] P.L. 1988, c.119
(C.17:28-1.4 et al), the commissioner shall, in the plan of
operation, establish procedures to govern the voluntary
writing of applicants and association insureds without
the utilization of the association. These procedures shall
include criteria identifying drivers who should be eligible

*EXPLANATION- Matter enclosed in bold-faced brackets
[thus] in the above bill is not enacted and is intended to be
omitted in the law.

Matter underlined thus is new matter.

Matter enclosed in superscript numerals has been adopted as
follows:

1 Senate SLI committee amendments adopted December 5,
1991.

2 Senate floor amendments adopted December 16, 1991.

for coverage in the voluntary market. Applicants and association insureds meeting these criteria shall be subject to assignment by the association to member companies, pursuant to an equitable apportionment procedure established in the plan of operation. The procedure shall give due consideration to the increase or decrease in the volume of private passenger automobile non-fleet exposures voluntarily written by member companies in this State since January 1, 1984.

b. (1) Pursuant to the procedures established in the plan of operation under subsection a. of this section, the commissioner shall establish a voluntary market quota, which shall not be less than 80% of the aggregate number of private passenger automobile non-fleet exposures written in the total private passenger automobile insurance market in this State on the effective date of [this 1988 amendatory and supplementary act] P.L.1988, c.119 (C.17:28-1.4 et al). The quota shall prescribe the number of voluntary market exposures which shall be written by member companies during the 12-month period beginning 80 days after the effective date of [this 1988 amendatory and supplementary act] P.L.1988, c.119 (C.17:28-1.4 et al).

(2) Within 30 days of the effective date of P.L. 1990, c.8 (C.17:33B-1 et al), the commissioner shall prescribe a second quota, which shall take effect immediately upon adoption by the commissioner and which shall not be less than 68% of the aggregate number of private passenger automobile non-fleet exposures written in the total private passenger automobile insurance market in this State on or before October 1, 1990. The quota shall prescribe the number of voluntary market exposures which shall be

written by member companies during the period described in this paragraph.

(3) (Deleted by amendment, P.L.1990, c.8.)

(4) (Deleted by amendment, P.L.1990, c.8.)

c. In the event that any of the quotas established by the commissioner pursuant to subsection b. of this section have not been met by the end of any applicable period, the commissioner shall direct the association to assign the balance of the exposures needed to meet the applicable quota to member companies in a manner consistent with the apportionment procedure established pursuant to subsection a. of this section. A member company which exceeded its apportionment share for the 12-month period prescribed pursuant to paragraph (1) of subsection b. of this section shall receive credit for the excess against the quota imposed pursuant to paragraph (2) of subsection b. of this section.

d. (Deleted by amendment, P.L.1990, c.8.)

e. For the purposes of this section, any exposure written in the voluntary market by an affiliate of the insurer to which an apportioned share has been assigned shall be credited against that share.

f. The total number of exposures written in the voluntary market, net of exposures cancelled or non-renewed, by a member company at the end of the applicable period shall be utilized in determining whether the member company has written its apportionment share in the voluntary market for purposes of complying with any quotas established by the commissioner pursuant to this section.

g. The commissioner may excuse a member company from meeting any of its obligations under this section that he determines would result in the member company being in an unsafe or unsound condition.

h. Any member company that does not write its apportionment share of any quota established by the commissioner pursuant to subsection b. or c. of this section within the applicable time period shall be precluded from nonrenewing automobile insurance policies pursuant to section 26 of P.L.1988, c.119 (C.17:29C-7.1) during the immediately following 12-month period.

i. In addition to the requirements of subsection a. of this section, the procedures governing the increase in voluntary market volume shall:

(1) establish guidelines and criteria for determining whether a person is a qualified applicant as defined in section 15 of P.L.1983, c.85 (C.17:30E-3), and procedures for the issuance of automobile insurance through the voluntary market to persons found not to be qualified applicants for association coverage, and for the referral of persons determined not to be eligible for association coverage to alternative residual market mechanisms:

(2) include provisions ensuring that servicing carriers do not obtain any unfair advantage over other member companies in the selection of qualified applicants and association insureds to be written as voluntary business:

(3) [neither prohibit nor require member companies to write association business through association producers of record, provided, however, that where a member company elects not to service such business through

the association producer of record, the procedures shall address the manner in which the association shall transfer the business to the member company, and shall establish reasonable compensation in an amount sufficient to offset the actual expenses incurred by the association producer in conjunction with the transfer which shall be paid by the association upon transfer of the business to the member company] ¹[provide that exposures assigned to member companies in accordance with subsection c. of this section as a result of the failure of the member company to meet an applicable quota shall be written through the association producer of record, notwithstanding the fact that the association producer of record is not a voluntary market producer of the member company assigned that exposure. In such case, the association producer of record shall retain complete control, possession and ownership of all records and renewals regarding the exposures written pursuant to this paragraph (3). The member company shall not use any such records, nor information it obtains in the normal course of business, to solicit direct renewal of the exposures, other insurance or any other products. The association producer of record shall be paid a commission by the member company on the exposures written by the member company through the association producer of record, and on all renewals thereof, at the same rate and on the same terms as the member company pays commissions for similar coverage to its voluntary market producers. If a member company provides its voluntary market producers with support services or other benefits in addition to a commission, and such support services or other benefits are not provided to the association producer of record, the commission paid to the association producer of record shall be

increased to make it equivalent to the value of the combination of commission and support services or other benefits paid or provided by the member company to its voluntary market producers. If the member company uses more than one commission schedule, rate or formula or provides different types of support services or other benefits to its voluntary market producers, it shall negotiate in good faith with the association producer of record so that the commission and support services and other benefits, if any, provided to the association producer of record are equivalent to that provided by the member company to its voluntary market producers for similar coverage. If a member company engages in the direct writing of exposures and neither it nor any affiliate has a commission schedule, rate or formula for the voluntary market, it shall pay the association producer of record a commission equivalent to the portion of the premium charged by the member company for voluntary market coverage that relates to its expenses for direct marketing, acquisition, servicing and related support staff, provided, however, that the commission shall be at least substantially equivalent to that paid by member companies that use commission schedules, rates or formulas. Notwithstanding any provision of this paragraph (3) to the contrary, if the member company uses premium rates of the Market Transition Facility for voluntary market exposures written through the association producer of record, the commission paid to the association producer of record shall be no less than that provided by the Market Transition Facility for such coverage] neither prohibit nor require member companies to write association business through association producers of record,² [provided,

however, that when association business is allocated, the procedures in this paragraph shall be observed] except as provided for in this paragraph².

(a) When an exposure assigned to a member company in accordance with subsection c. of this section, as a result of the failure of the member company to meet an applicable quota, is written by the member company assigned the exposure, the association producer of record shall have the right to service that business, which shall include all renewals thereof, and shall be entitled to a commission for that service in accordance with subparagraph (c) of this paragraph.

(b) This association producer of record shall retain²complete² control²[and]² possession²and ownership² of all records and²[the right and entitlement to]² renewals regarding exposures assigned pursuant to subsection c. of this section, provided, however, that the member company may maintain such records as are provided to it under the procedure established by subsection a. of this section. A member company that acquires access to records pursuant to this subparagraph shall not share any such records with any other producer or use any such records to solicit direct renewal of the business, a change in producer of record, other insurance products or any other products.

(c) The association producer of record shall be paid a commission by the member company on the business serviced by the association producer of record pursuant to this paragraph. That commission shall be paid at a percentage rate no less than that being paid by the Market Transition Facility on July 1, 1991.

(d) A copy of every notice, other than bills, and including renewal declarations, change endorsements, cancellations and reinstatements, and the corresponding payment schedules included therein, correspondence, claims checks and acknowledgements, sent to an insured by a member company with respect to business covered by this paragraph, shall be sent to the association producer of record.

(e) This paragraph shall be applicable only to exposures assigned to member companies in accordance with subsection c. of this section as a result of the failure by the member company to meet an applicable quota ²[and shall not apply beyond three years after the enactment date of this 1991 amendatory act.]² This paragraph shall not constitute the grant of an agency contract by the member company to the association producer of record authorizing the association producer of record to write new business through the member company; provided, however, that the association producer of record shall have the authority to provide the usual and customary servicing of the business subject to this paragraph, including adding new and replacement vehicles and adding or changing coverages on the business.

(f) Nothing in this paragraph shall deprive an insured of the right to designate a producer of record other than the association producer of record. Upon that designation, the rights of the association producer of record under this paragraph shall terminate. Notwithstanding any provision in this paragraph, the rights of the association producer of record under this paragraph shall terminate in the event of the producer's insolvency,

gross and willful misconduct, fraud or license revocation¹; and

(4) provide for financial disincentives to applicants who, without good cause, reapply for coverage in the association after being placed in the voluntary market. (cf: P.L.1990, c.8, s.20)

2. Section 88 of P.L.1990, c.8 (C.17:33B-11) is amended to read as follows:

88. a. There is created a Market Transition Facility to be operated by the Commissioner of Insurance pursuant to the provisions of this section. Every insurer authorized to transact automobile insurance in this State shall be a member of the facility and shall share in its profits and losses as provided by the commissioner pursuant to the provisions of subsection d. of this section.

b. The commissioner shall, within 30 days of the effective date of [this 1990 amendatory and supplementary act] P.L.1990, c.8 (C.17:33B-1 et al), appoint a Market Transition Facility Advisory Board which shall be comprised of six members, one of whom shall represent member companies organized on a mutual basis, one of whom shall represent member companies organized on a stock basis, one of whom shall represent servicing carriers, one of whom shall represent insurance producers, one of whom shall be a qualified actuary and one of whom shall represent the public. Advisory board members shall serve for the duration of the facility or until such time as their successor is appointed. Advisory board members shall not be compensated for their services but shall be reimbursed by the facility for any necessary and reasonable

expenses incurred in performance of their duties as members of the advisory board.

c. The facility shall arrange for the issuance and renewal of automobile insurance policies for the period commencing October 1, 1990 and ending September 30, 1992 pursuant to a plan of operation promulgated by the commissioner in consultation with the advisory board. The facility shall not issue or renew any policies of automobile insurance on or after October 1, 1992. The plan shall provide:

(1) The applicable levels of coverage available through the facility;

(2) That the premiums payable on policies issued by the facility shall be based on rates applicable to persons insured by the New Jersey Automobile Full Insurance Underwriting Association on September 30, 1990 but shall not incorporate the rates applicable under section 25 of P.L.1983, c.65 (C.17:30E-13) and section 22 of P.L.1988, c.119 (C.17:30E-13.1). However, the applicable rates for those insureds who do not qualify as eligible persons as provided in section 25 of [this 1990 amendatory and supplementary act] P.L.1990, c.8 (C.17:33B-13) shall be those set by the plan for the provision of automobile insurance established pursuant to section 1 of P.L.1970, c.215 (C.17:29D-1);

(3) Procedures for the filing and approval of changes in rates applicable to policies issued or renewed by the facility;

(4) For the issuance and renewal of automobile insurance through servicing carriers under contract with

the New Jersey Automobile Full Insurance Underwriting Association pursuant to the provisions of section 24 of P.L.1983, c.65 (C.17:30E-12), utilizing, at the discretion of the commissioner, the staff of the association;

(5) Procedures for the depopulation of the facility which shall provide that: on or after April 1, 1991 no more than 29% of the aggregate number of private passenger non-fleet exposures written in this State shall be written by the facility and the New Jersey Automobile Full Insurance Underwriting Association created by P.L.1983, c.65 (C.17:30E-1 et seq.); on or after October 1, 1991 no more than 20% of the aggregate number of private passenger non-fleet exposures written in this State shall be written by the facility; on or after April 1, 1992 no more than 10% of the aggregate number of private passenger non-fleet exposures written in the State shall be written by the facility; and on or after October 1, 1992, 0% of the aggregate number of private passenger non-fleet exposures written in this State shall be written by the facility. In establishing the quotas set forth above, the plan shall prescribe the number of voluntary market exposures which shall be written during each six-month period set forth in this paragraph in a manner consistent with the apportionment procedure established pursuant to subsection a. of section 26 of P.L.1983, c.65 (C.17:30E-14). In the event that any of the quotas established pursuant to this paragraph have not been met by the end of the applicable period, the commissioner shall direct the facility to assign the balance of the exposures needed to meet the applicable quota to member companies pursuant to the apportionment procedure. A member company which exceeds its apportionment share for

any six-month period set forth in this paragraph shall receive credit for the excess against the following period's obligation. The commissioner may excuse a member company from meeting its obligations under the depopulation procedures if he determines that the company would be placed in an unsafe or unsound condition.

¹[Exposures assigned to member companies in accordance with this paragraph (5) as a result of the failure of the member company to meet an applicable quota shall be written through the Market Transition Facility producer of record, notwithstanding the fact that the facility producer of record is not a voluntary market producer of the member company assigned that exposure. In such case, the facility producer of record shall retain complete control, possession and ownership of all records and renewals regarding the exposures written pursuant to this paragraph (6). The member company shall not use any such records, nor information it obtains in the normal course of business, to solicit direct renewal of the exposures, other insurance or any other products. The facility producer of record shall be paid a commission by the member company on the exposures written by the member company through the facility producer of record, and on all renewals thereof, at the same rate and on the same terms as the member company pays commissions on similar coverage to its voluntary market producers. If a member company provides its voluntary market producers with support services or other benefits in addition to a commission, and such support services or other benefits are not provided to the facility producer of record, the commission paid to the facility producer of record shall be increased to make it equivalent to the value of the

combination of commission and support services or other benefits paid or provided by the member company to its voluntary market producers. If the member company uses more than one commission schedule, rate of formula or provides different types of support services or other benefits to its voluntary market producers, it shall negotiate in good faith with the facility producer of record so that the commission and support services and other benefits, if any, provided to the facility producer of record are equivalent to that provided by the member company to its voluntary market producers for similar coverage. If a member company engages in the direct writing of exposures and neither it nor any affiliate has a commission schedule, rate of formula for the voluntary market, it shall pay the facility producer of record a commission equivalent to the portion of the premium charged by the member company on voluntary market coverage that relates to its expenses for direct marketing, acquisition, servicing and related support staff, provided, however, that the commission shall be at least substantially equivalent to that paid by member companies that use commission schedules, rates or formulas. Notwithstanding any provision of this paragraph (5) to the contrary, if the member company uses premium rates of the Market Transition Facility for voluntary market exposures written through the facility producer of record, the commission paid to the facility producer of record shall be no less than that provided by the Market Transition Facility for such coverage] When an exposure is assigned to a member company under this paragraph as a result of the failure of the member company to meet an applicable

quota, but only in such circumstances, the following shall apply:

(a) When an assigned exposure is written by the member company assigned the exposure, the facility producer of record shall have the right to service that business, which shall include all renewals thereof, and shall be entitled to a commission for that service in accordance with subparagraph (c) of this paragraph:

(b) The facility producer of record shall retain ²complete² control ²[and],² possession ²and ownership² of all records and ²[the right and entitlement to]² renewals regarding exposures assigned pursuant to this paragraph, provided, however, that the member company may maintain such records as are provided to it under the procedure established by subsection a, of section 26 of P.L.1983, c.65 (C.17:30E-14). A member company that acquires access to records pursuant to that subsection shall not share any such records with any other producer or use any such records to solicit direct renewal of the business, a change in producer of record, other insurance products or any other products;

(c) The facility producer of record shall be paid a commission by the member company on the business serviced by the facility producer of record pursuant to this paragraph. That commission shall be paid at a percentage rate no less than that being paid by the Market Transition Facility on July 1, 1991;

(d) A copy of every notice, other than bills, and including renewal declarations, change endorsements, cancellations and reinstatements, and the corresponding payment schedules included therein, correspondence,

claims checks and acknowledgments, sent to an insured by a member company with respect to business covered by this paragraph, shall be sent to the facility producer of record;

(e) The procedure established in subparagraphs (a), (b), (c), (d), (e) and (f) of this paragraph shall be applicable only to exposures assigned to member companies in accordance with this paragraph as a result of the failure by the member company to meet an applicable quota²[and shall not apply beyond three years after the enactment date of this 1991 amendatory act]². This paragraph shall not constitute the grant of an agency contract by the member company to the facility producer of record authorizing the facility producer of record to write new business through the member company; provided, however, that the facility producer of record shall have the authority to provide the usual and customary servicing of the business subject to this paragraph, including adding new and replacement vehicles and adding or changing coverages on the business; and

(f) Nothing in the paragraph shall deprive an insured of the right to designate a producer of record other than the facility producer of record. Upon that designation, the rights of the facility producer of record under this paragraph shall terminate. Notwithstanding any provision in this paragraph, the rights of the facility producer of record under this paragraph shall terminate in the event of the producer's insolvency, gross and willful misconduct, fraud or license revocation¹;

(6) A schedule for the payment of premiums on an installment basis. Any installment payment schedule for

policies issued for a one year period shall provide for installment payments during a period of not less than nine months;

(7) That no policy issued by the facility may be cancelled for nonpayment of premium unless written notice is provided at least 15 days prior to the effective date of cancellation accompanied by the reason for cancellation. Notice shall be provided to the named insured and the producer of record at their last known addresses;

(8) Provide for notification of the named insured and the producer of record at their last known addresses no later than 15 days after the nonrenewal of a facility policy of such nonrenewal; and

(9) Such other provisions as are deemed necessary for the operation of the facility.

d. The commissioner shall apportion any profits or losses of the facility among member companies based on each company's apportionment share as determined for purposes of depopulation pursuant to subsection a. of section 26 of P.L.1983, c.65 (C.17:30E-14).

e. The facility shall be subject to the provisions of P.L.1945. c.132 (C.54:18A-1 et seq.).

(cf; P.L.1990, c.8 § 88)

3. This act shall take effect immediately and shall be retroactive to March 12, 1990.

INSURANCE

Provides that producers of record must be used for automobile insurance coverage assigned to voluntary market insurers under depopulation plans.

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[LOGO]

State of New Jersey
DEPARTMENT OF INSURANCE

December 31, 1991

CN 325
TRENTON 08625-0325

Mr. Richard Cibula
Allstate Insurance Company
Allstate Plaza E-3
Northbrook, IL 60062

**RE: IN THE MATTER OF THE ASSIGNMENT
OF EXPOSURES TO Allstate Insurance
Company, A MEMBER COMPANY OF
THE NEW JERSEY AUTOMOBILE FULL
INSURANCE UNDERWRITING ASSO-
CIATION AND THE MARKET TRANSI-
TION FACILITY OF NEW JERSEY,
PURSUANT TO THE VOLUNTARY MAR-
KET PLACEMENT PROGRAM
A91-354**

Dear Mr. Cibula:

Enclosed is an Order issued by the Commissioner of Insurance with regard to above-captioned matter.

The Department of Insurance will schedule a meeting for member companies and the servicing carriers in the next week to ten days. If you have any questions, please contact the Auto Residual Market Unit at 609-292-4240.

Very truly yours,

/s/ Jean M. Bickal
Jean M. Bickal
Regulatory Officer
Auto Residual Market Unit

ORDER NO.: A91-354

STATE OF NEW JERSEY
DEPARTMENT OF INSURANCE

IN THE MATTER OF THE)
ASSIGNMENT OF EXPOSURES TO)
ALLSTATE INSURANCE COMPANY,)
A MEMBER OF THE NEW JERSEY) ORDER
AUTOMOBILE FULL INSURANCE)
UNDERWRITING ASSOCIATION)
AND THE MARKET TRANSITION)
FACILITY OF NEW JERSEY,)
PURSUANT TO THE MANDATORY)
DEPOPULATION ASSIGNMENT PLAN)

This matter having been opened by the Commissioner of Insurance of the State of New Jersey ("Commissioner") pursuant to the authority of *N.J.S.A. 17:1C-1 et seq.*, *N.J.S.A. 17:30E-1 et seq.*, *N.J.S.A. 17:33B-1 et seq.*, and all powers expressed or implied therein; and

IT APPEARING that *N.J.S.A. 17:30E-14a* requires the Commissioner to establish procedures in the Plan of Operation ("Plan") of the New Jersey Automobile Full Insurance Underwriting Association ("Association") to govern the voluntary writings of applicants and Association insureds without utilization of the Association; and

IT FURTHER APPEARING that pursuant *N.J.S.A. 17:30E-7*, the Association ceased the issuance or renewal of automobile insurance policies effective October 1, 1990, and pursuant to *N.J.S.A. 17:30E-1 et seq.*, and *17:33B-1 et seq.*, the Association has been succeeded in function and responsibility by the Market Transition Facility ("MTF"); and

IT FURTHER APPEARING that N.J.S.A. 17:33B-11c(5) requires the Commissioner to establish a Plan of Operation for the MTF which provides procedures for the depopulation of the MTF in accordance with the provisions of the statute; and

IT FURTHER APPEARING that N.J.S.A. 17:30E-14c and 17:33B-11c(5), and the Association and MTF Plans of Operation, require the Commissioner to direct the Association and MTF to assign to member companies the balance of exposures needed to meet the applicable quota in the event that any quota established by the Commissioner was not met by the end of the applicable quota period; and

IT FURTHER APPEARING that the member companies of the Association were notified by letter on or about May 15, 1990 of their apportionment share for the depopulation quota period ending September 30, 1990; and

IT FURTHER APPEARING that the depopulation quota established by the Commissioner for the period ending September 30, 1990 was not met according to the quarterly reports filed by the member companies with the Department of Insurance listing in force exposures by territory as of September 30, 1990; and

IT FURTHER APPEARING that Allstate Insurance Company ("Allstate") failed to meet its assigned apportionment share by 32,687 exposures as of September 30, 1990; and

IT FURTHER APPEARING that the Commissioner ordered in Order No. A91-111 the Association and MTF

to assign exposures to Allstate in accordance with the provisions of the Mandatory Depopulation Assignment Plan attached thereto; and

IT FURTHER APPEARING that as a result of a decision of the Superior Court of New Jersey, Appellate Division in *In the Matter of the Assignment of Exposures to the Aetna Casualty And Surety Company, Allstate Insurance Company and Colonial Penn Insurance Company* 248 NJ Super. 367 (App. Div. 1991), ("*Aetna*") the Mandatory Depopulation Assignment Plan established by Order No. A91-111 was not implemented; and

IT FURTHER APPEARING that the Association had no policies in force as of October 1, 1991; and

IT FURTHER APPEARING that it is therefore necessary to establish a new Mandatory Depopulation Assignment Plan to provide for the assignment of MTF exposures consistent with N.J.S.A. 17:30E-1 *et seq.*, 17:33B-11c(5), and the decision of the Court in *Aetna*; and to rescind formally Order No. A91-111.

IT IS on this 31st day of December, 1991,

ORDERED that:

1. The MTF shall assign to Allstate a sufficient number of exposures from MTF policies expiring on or after April 1, 1992 to meet Allstate's assigned apportionment share in accordance with the provisions of the Mandatory Depopulation Assignment Plan (Revision No. 2, December 27, 1991) as set forth in Exhibit 1 and supplementary Exhibits 2 through 5, attached hereto and made a part hereof;

2. Allstate shall comply with the provisions of the Mandatory Depopulation Assignment Plan;

3. Allstate shall be precluded from requiring the assigned MTF policyholder to obtain or maintain membership or qualification for membership in any club, group or organization as a condition for providing automobile insurance coverage, including the payment of dues, membership fees, or other charges;

4. Allstate shall be fined \$2,000.00 for every offer of automobile insurance coverage or policy of automobile insurance which Allstate fails to make or issue at least thirty (30) days prior to the expiration date of the assigned MTF policy. Pursuant to N.J.S.A. 17:30E-17a, all fines shall be collected and enforced in accordance with N.J.S.A. 2A:58-1 *et seq.* (the "Penalty Enforcement Law");

5. Allstate shall be subject to any other penalty provision of N.J.S.A. 17:30E-17, and any other penalties authorized by law, if Allstate fails to comply with the terms of this Order and the provisions of the Mandatory Depopulation Assignment Plan; and

6. Order No. A91-111 is hereby rescinded.

12/31/91
Date

/s/ Samuel F. Fortunato
Samuel F. Fortunato
Commissioner

JC40/ORDERS

EXHIBIT 1

MANDATORY DEPOPULATION ASSIGNMENT PLAN

The following procedures shall govern the assignment of exposures by the Market Transition Facility of New Jersey ("MTF") to every member company ordered by the Commissioner of Insurance of the State of New Jersey ("Commissioner") to receive such assignments as a result of the member company's failure to write its apportionment share established by the Commissioner for the depopulation quota period which ended September 30, 1990:

1. Assignment of private passenger automobile non-fleet exposures ("exposures") shall be made from those rating territories indicated below. For purposes of this Mandatory Depopulation Assignment Plan ("MDAP"), these rating territories shall be referred to as the territories subject to assignment.

<u>Rating Territory No.</u>	<u>Brief Territory Description</u>	<u>Target Territory Assignment Percentages</u>
27	Cumberland/Ocean/ Atlantic	16.34%
14	Gloucester/Salem/ Burlington	12.98%
40	New Brunswick	10.18%
03	Paterson	9.55%
01	Jersey City	9.01%
04	Elizabeth	7.75%
16	Long Branch	6.71%
11	South Bergen County	5.98%
02	Newark	4.54%

13	Camden County	
	(Balance)	3.80%
08	Perth Amboy	3.38%
22	Newark Semi-Suburban	2.75%
38	East Orange/Orange	2.12%
07	Camden	1.67%
23	Hudson County	1.53%
05	Bayonne	1.20%
19	Atlantic City	0.49%

2. The quarterly in-force exposure reports filed by the member companies for the period ending September 30, 1990, after adjustments were made for exemptions and revisions to in-force exposures, indicate that those member companies that failed to write their apportionment shares, in the aggregate, fell short by 204,050 exposures. The assignment of exposures to these member companies shall be made from the territories subject to assignment.

3. The number of exposures assigned to each member company may be increased by an acceptance factor of up to 25 percent. The resulting number shall be rounded off and be referred to as the member company's individual assignment goal. The sum of all the member company's individual assignment goals shall be referred to as the overall assignment goal. It is the expectation of the Department that not every offer of coverage made by a member company to its assigned policyholders will be accepted. This expectation is based on the dynamic aspect of the New Jersey automobile insurance market. (i.e., MTF policyholders independently seeking coverage with a voluntary insurer, competition among member companies to write additional new business in order to meet future depopulation quotas, MTF policyholders leaving

New Jersey) and the requirement that member companies only write eligible persons.

4. The number of exposures to be assigned to each member company per territory shall be determined as follows:

a. An assignment percentage shall be determined by dividing the overall assignment goal by the total number of available MTF exposures from the territories subject to assignment. The methodology will result in an equal percentage of MTF exposures being assigned from each territory subject to assignment.

b. The target number of exposures to be assigned from each territory subject to assignment shall be determined by multiplying the number of MTF exposures available for that territory (as of the most recent quarterly in-force exposure report) by the assignment percentage.

c. A target territory assignment percentage shall be determined for each territory subject to assignment by dividing the target number of exposures to be assigned from such territory by the overall assignment goal.

d. The target number of exposures to be assigned to each member company from each territory subject to assignment shall be determined by multiplying the target territory assignment percentage by the member company's individual assignment goal.

e. The monthly number of exposures to be assigned to each member company from each territory subject to assignment shall be determined by dividing the

target number of exposures to be assigned to the member company for the territory subject to assignment by twelve (12). The resulting number shall be rounded off.

f. The resulting monthly numbers for each member company shall be adjusted by a fitting algorithm to ensure that a sufficient number of exposures are assigned to meet the member company's individual assignment goal.

g. The number of exposures to be assigned to each member company shall be the sum of all monthly exposures to be assigned to that member company from each territory subject to assignment.

5. For the purposes of the MDAP, offer of coverage means making an offer of automobile insurance coverage at least 30 days prior to the expiration date of the assigned MTF automobile insurance policy (for those member companies that make offers of coverage to applicant prior to the issuance of the automobile insurance policy) or issuing a policy of automobile insurance at least 30 days prior to the expiration date of the assigned MTF automobile insurance policy (for those member companies that do not make offers of coverage to applicants).

6. a. The member company shall make offers of coverage to every person listed on the assigned MTF policy, who the member company has determined to be an eligible person in accordance with item 18 below, at least 30 days prior to the expiration date of the assigned MTF policy (*i.e.*, upon renewal of the MTF policy). The

offer of coverage shall include, for each assigned exposure, the coverages, limits, options and deductibles transferred to the member company under item 18 below and Policyholder Assignment Notice attached hereto as Exhibit 2A, in accordance with item 9 below. The offer of coverage shall be contained in an envelope appropriately emboldened on the outside with the statement "IMPORTANT AUTO INSURANCE MATERIALS ENCLOSED."

b. The member company shall include with the offer of coverage the statements of privacy practices required by law (*e.g.*, Insurance Information Practices Act (N.J.S.A. 17:23A-1 *et seq.*); Fair Credit Reporting Act). The member company may include an authorization form to be signed by the assigned MTF policyholder in order to obtain investigative consumer reports. Provided, however, that the failure of the assigned policyholder to return a signed authorization form shall not be grounds for the member company to decline coverage, or cancel, nonrenew or otherwise terminate the policy during the one (1) year period required by item 12 below.

7. The member company is expressly prohibited from requiring the assigned MTF policyholder to obtain or maintain membership or qualification for membership as a condition for providing automobile insurance coverage, including, but not limited to, charging dues, membership fees or other charges.

8. The member company shall continue to make offers of coverage to all eligible persons on assigned MTF policies even after the member company has written sufficient exposures to meet its apportionment share shortfall. Any exposures written in excess of the apportion-

ment share shortfall may be used by the member company toward the fulfillment of its next apportionment share.

9. a. If the underwriting review by the member company determines that some or all of the drivers on the policy transferred from the MTF are eligible persons, the member company shall mail the Policyholder Assignment Notice attached hereto as Exhibit 2A with the offer of coverage as required by item 6 above. The Policyholder Assignment Notice must list *all* policyholders and operators on the MTF policy as either eligible or ineligible.

b. If the underwriting review by the member company determines that all of the drivers on the assigned policy are *not* eligible, the member company shall send the Policyholder Ineligibility Notice attached hereto as Exhibit 2B to the assigned MTF policyholder.

c. Copies of the Policyholder Assignment Notice or Policyholder Ineligibility Notice (hereafter, Notices) sent to the policyholder, whether Exhibit 2A or 2B shall be sent simultaneously to the Servicing Carrier and the Producer of Record.

d. Except for format changes, any change to the Notices must be approved by the Automobile Residual Market Unit of the Department before such notice is mailed to any MTF policyholder (*e.g.*, changes to the required information, adding additional information to the notice, changes in type pointsize). For purposes of this paragraph, format change means only the realignment of the required information to accommodate the various data processing systems of the member companies.

e. The type size used in the Notices shall be at least 10-point. The type style used in the Notices shall be the same type style used by the member company in the Buyer's Guide (*N.J.A.C. 11:3-15.1 et seq.*). The size of the paper shall be eight and one-half inches by eleven inches. The member company may print the required Notices on both sides of the paper.

10. It is the responsibility of the member company to be able, upon request, to demonstrate to the satisfaction of the Department or MTF that an offer of coverage and/or the correct Notice was mailed to the assigned MTF policyholder.

11. The member company shall offer the same or equivalent automobile insurance coverage that was afforded under the MTF policy to every assigned MTF policyholder where the member company has rates and rules for such coverage filed and approved by the Department. Where the member company does not have rates and rules filed and approved by the Department for the same or equivalent coverage presently afforded the assigned policyholder under the MTF policy, the member company shall offer to the assigned MTF policyholder the next broadest coverage for which the member company has rates and rules filed and approved by the Department. The member company is expressly prohibited from offering less coverage to the assigned policyholder than the coverage afforded to such policyholder under the MTF policy.

The following examples are provided for illustration purposes only:

Example 1: The MTF policyholder presently has \$25,000/\$50,000/\$10,000 split limits of liability coverage. However, the member company that has been assigned this policyholder only writes combined single limit of liability coverage and only has rules and rates filed and approved by the Department for this type coverage. Therefore, the member company must offer the MTF policyholder a combined single limit of liability coverage which is equal to the bodily injury occurrence limit and the property damage occurrence limit added together or the next broadest available coverage (e.g., \$75,000, but in no event less than \$60,000).

Example 2: The MTF policyholder presently has \$25,000/\$50,000/\$10,000 split limits of liability coverage. The member company that has been assigned this policyholder only writes combined single limit of liability coverage and offers \$100,000 combined single limit of liability coverage as the minimum coverage to its voluntary insureds. However, the member company has rates and rules filed and approved by the Department for combined single limit of liability coverage for amounts less than \$100,000. Therefore, the member company must offer the MTF policyholder a combined single limit of liability coverage which is equal to the bodily injury occurrence limit and the property damage occurrence limit added together or the next broadest available coverage, but less than \$100,000 (e.g., \$75,000, but in no event less than \$60,000).

Example 3: The MTF policyholder presently has \$25,000/\$50,000/\$10,000 split limits of liability coverage. The member company that has been assigned this policyholder only writes combined single limit of liability

coverage and offers \$100,000 combined single limit of liability coverage as the minimum coverage to its voluntary insureds. The member company does not have any rates and rules filed and approved by the Department for amounts of combined single limit of liability coverage less than \$100,000. Therefore, the member company must offer the MTF policyholder \$100,000 combined single limit of liability coverage.

Example 4: The MTF policyholder presently has \$75,000 combined single limits of liability coverage. The member company that has been assigned this policyholder writes both split limits and combined single limit of liability coverage and has rates and rules filed and approved by the Department for both types of coverage. Therefore, the member company must offer the MTF policyholder \$75,000 combined single limit of liability coverage and not a split limits policy.

Example 5: The MTF policyholder presently has \$100,000 combined single limit of liability coverage. The member company that has been assigned this policyholder writes only split limits of liability coverage and only has rates and rules filed and approved by the Department for this type of coverage. Therefore, the member company must offer the MTF policyholder split limits of liability coverage with a bodily injury per person limit equal to the combined single limit of liability coverage or the next broadest available coverage (e.g., \$100,000/\$300,000/\$50,000). (Note: All conversions of combined single limit of liability coverage should be handled in the same manner, except a \$35,000 combined single limits policy. In this particular case, the member

company shall offer \$15,000/\$30,000/\$5,000 split limits of liability coverage.)

12. a. Upon acceptance of the offer of coverage by the MTF policyholder, the member company shall, at a minimum, write and service the assigned exposure(s) for a period of one (1) year from the policy expiration date of the assigned MTF policy, regardless of the member company's customary policy term (*e.g.*, 6 months). The member company shall provide coverage or continue to provide coverage to the assigned insured even though the assigned insured becomes ineligible after the completion of the underwriting review period permitted by item 18 below. The member company may nonrenew the policy of any ineligible person at the expiration of the 12 month policy period in accordance with the applicable New Jersey statutes and regulations in effect at the time of such nonrenewal.

b. For purposes of this paragraph, writing and servicing the assigned exposure shall be given the broadest possible meaning while the policy is in force, including, but not limited to, (i) adjusting claims resulting from accidents and (ii) adding or deleting vehicles, adding or deleting eligible drivers and adding, changing or deleting coverages, limits, options or deductibles when requested to do so by the assigned policyholder. The member company shall provide any change properly requested by the assigned policyholder during the mandatory one (1) year assignment period for which the member company has rates and rules filed and approved by the Department. Essentially, the assigned MTF policyholder shall have the same rights during this one (1) year period as if the policy were insured through the MTF.

13. Upon acceptance of the offer of coverage, the member company shall be permitted to charge additional premium in accordance with its rates and rules filed and approved by the Department based on subsequent information supplied to the member company (e.g., undisclosed motor vehicle violations and/or accidents, change in the number of miles driven to work due to new employment or change in coverage requested by policyholder).

14. a. Included with the offer of coverage or upon acceptance of the offer of coverage by the assigned MTF policyholder, the member company shall provide the assigned MTF policyholder with a Coverage Selection Form and the New Jersey Auto Insurance Buyer's Guide ("Buyer's Guide"). The Coverage Selection Form shall be filled in by the member company with the applicable information provided to the member company by computer tape in accordance with item 18 below (e.g., policyholder name, coverages, limits, options and deductibles). The member company shall ask the assigned MTF policyholder to sign and return the Coverage Selection Form. The assigned policyholder has the right to elect different coverages, limits, options and deductibles.

b. Where the assigned MTF policyholder has accepted coverage with the member company but has failed to return a signed Coverage Selection Form, the member company shall send a second completed Coverage Selection Form and Buyer's Guide to the assigned policyholder in accordance with the proof of mailing procedures set forth in N.J.S.A. 17:29C-10. The second Coverage Selection Form and Buyer's Guide shall be

accompanied by the policyholder notice attached hereto as Exhibit 3. This notice shall inform the policyholder that failure to return a signed Coverage Selection Form to the member company will result in the tort option and the physical damage deductibles being changed to the statutory defaults (*i.e.*, lawsuit threshold, \$500 physical damage deductibles). The policyholder notice shall follow the same requirements set forth under item 9 above (*i.e.*, type size, type style, changes to the notice, paper size). Provided, however, that the failure of the assigned policyholder to return a signed Coverage Selection Form shall not be grounds for the member company to cancel or otherwise terminate the policy.

15. The member company shall comply with all applicable New Jersey statutes and regulations in providing coverage to the assigned MTF policyholder (*e.g.*, mandatory physical damage inspection).

16. In providing coverage to the assigned MTF policyholder, the member company shall issue the policy in accordance with its voluntary business practices to the extent practicable. Provided, however, that the member company shall not be permitted to utilize its voluntary business practices during the one (1) year period required by item 12 above where such practices are more restrictive than the standards utilized by the MTF.

For example, the MTF presently permits the policyholder to pay the annual premium in six (6) installment payments. The last payment is due 270 days after the effective date of the policy. A member company cannot use its voluntary installment payment plan if such plan requires the assigned policyholder to pay the annual

premium in less than six (6) installments or less than 270 days from the effective date of the policy.

17. Except for the reasons set forth in *N.J.S.A. 17:29C-7(A)*, the member company shall not be permitted to decline coverage or cancel, nonrenew or otherwise terminate the assigned exposure during the one (1) year period required by item 12 above. Upon expiration of this one (1) year period, the member company may cancel or nonrenew the assigned exposure in accordance with New Jersey statutes and regulations in effect at the time of such cancellation or nonrenewal.

18. a. Each month for twelve (12) consecutive months after the effective start date of the MDAP, each member company that is subject to mandatory assignment of exposures shall receive policy information from an assigned MTF servicing carrier at least 75 days prior to the expiration date of the assigned MTF policies. Each member company shall receive, by overnight or priority mail, their monthly mandatory assignments by computer tape. Where the due date for the delivery of the computer tape falls on a weekend or holiday, the assigned MTF servicing carrier shall deliver the monthly computer tape by the close of business of the next business day. The type of computer tape (i.e., cartridge or reel) utilized for the purposes of this MDAP shall be left to the sole discretion of the assigned MTF servicing carrier. The MTF servicing carrier shall provide the policy information to the member company in the record format set forth in the Exhibit 5.

For purposes of illustration only, assume the MDAP requires member companies to provide coverage to

eligible MTF persons whose policies expire during the month of April, 1992. On or before January 15, 1992, the assigned MTF servicing carrier will deliver to the member company a computer tape listing all the assigned MTF policies due to expire during the month of April, 1992.

b. Within three (3) calendar days of receipt of the monthly computer tape, the member company shall evaluate the computer tape. The member company shall notify both the assigned MTF servicing carrier and the Department of any problems encountered by the member company with the monthly computer tape (e.g., unreadable tape, missing policy information essential to the proper rating of the policy). To the extent practicable, the assigned MTF servicing carrier shall resolve all problems encountered by the member company with such tape within three (3) calendar days from the date of notification of such problems (e.g., resubmit a new tape). Where the third calendar day falls on a weekend or holiday, the problem shall be resolved by the close of business of the next business day.

c. The member company shall be permitted to perform an underwriting review of the assigned MTF policies received by computer tape pursuant to paragraph (a) above to determine if any assigned person is not an eligible person as defined in *N.J.A.C. 11:3-34.1 et seq.* For the purposes of the MDAP, the definition of eligible person shall *not* include membership qualifications or fees as set forth in *N.J.A.C. 11:3-34.4(a)(7)*. See also, *N.J.S.A. 17:33B-26*. In determining whether a person listed on an assigned MTF policy is not an eligible person, the member company shall utilize the standards set

forth in *N.J.A.C. 11:3-8.4(a)*. Essentially, the member company is not required to offer coverage to any person listed on the assigned MTF policy that the member company has determined not to be an eligible person in accordance with the applicable standards. The member company, however, shall offer coverage to all eligible persons listed on the assigned MTF policy.

d. All underwriting reviews shall be completed by the member company within 60 days of receipt of the computer tape from assigned MTF servicing carrier. For purposes of this MDAP, 60 days means two (2) calendar months.

For purposes of illustration only, assume the MDAP requires member companies to provide coverage to eligible persons whose MTF policy expires during the month of April, 1992. The member company receives its monthly computer tape from its assigned MTF servicing carrier on or before January 15, 1992 containing all the assigned MTF policies due to expire during April, 1992. All underwriting reviews shall be completed by the member company by the close of business on March 15, 1992. In order to make offers of coverage at least 30 days prior to the expiration date of the MTF policy as required by paragraph 6 above, it is assumed that the member company will begin issuing offers of coverage on or before March 1, 1992 for those MTF policies expiring April 1 through April 15, 1992 and begin issuing offers of coverage on or before March 15, 1992 for those MTF policies expiring April 16 through April 30, 1992.

e. The member companies are encouraged to exchange test computer tapes with its assigned MTF servicing carrier prior to the start of the MDAP.

f. The member companies shall complete any request form provided by its assigned MTF servicing carrier. The form and content of the form shall be prescribed by MTF servicing carrier. The purpose of this form is to inform MTF servicing carrier where MTF servicing carrier is to send the monthly computer tapes and the name, title, telephone number and facsimile number of a contact person for the member company. Where the member company intends to use a third party, subcontractor, pooling company and/or other entity to write the mandatory assignments on its behalf, the member company shall also supply the name, title, telephone number and facsimile number for a contact person at the third party, subcontractor, pooling company and/or other entity.

h. The use of a third party, subcontractor, pooling company and/or other type entity to write the mandatory assignments on behalf of the member company shall *not* relieve the member company of its responsibilities under the MDAP.

19. All member companies shall be permitted to use MTF rates and rules as authorized by N.J.S.A. 17:33B-11(c)(2) and N.J.S.A. 17:33B-12 for the exposures mandatorily assigned from the MTF. The member company shall notify the Department of its election to use or cease using MTF rates in accordance with the requirements set forth in Department Order No. A91-339. The applicable MTF rule and rate pages shall be made available to member companies by the MTF for a reasonable fee to be determined by the MTF.

20. The member company shall be permitted to use prospectively rates and rules filed and approved by the Department after the start of the MDAP. Provided, however, member companies that issue six (6) month policies shall be precluded from using the new approved rates and rules in issuing the second six (6) month policy, but rather shall use the same rates and rules which were used in issuing the first six (6) month policy.

21. The producer of the assigned MTF policy shall not be permitted to place any new business with the member company, unless the producer and member company enter into a voluntary agreement. Furthermore, the member company is under no obligation to service the assigned business through, or pay a commission to, the producer of record of the assigned MTF policy.

22. Each quarter after the effective start date of the MDAP until the quarter ending June 30, 1994, each member company shall report separately, by territory, the following information to the Department concerning the exposures assigned to it under this MDAP:

a. The number of policies, insureds and exposures received from its assigned MTF servicing carrier;

b. The number of persons listed on the assigned MTF policies who the member company has determined not to be eligible persons;

c. The number of offers of coverage issued for eligible persons;

d. The number of offers of coverage accepted by eligible persons and the number of exposures in force;

e. The number of policies which are canceled or nonrenewed. Whenever a policy is canceled or nonrenewed, the member company shall provide the Department with a separate report from that required by this provision indicating the policyholder's name, address (including zip code), telephone number (including area code), policy number and the specific reason why such policy was canceled or nonrenewed; and

f. The number of exposures which are canceled or nonrenewed.

23. The information required by item 22 above shall be delivered and received by the Department no later than the close of business on the 20th calendar day of the month following the close of the calendar quarter. Where the 20th calendar day falls on a weekend or holiday, the report is due by the close of the next business day. The report and the content of the report required by item 22 above shall be prescribed by the Department and is attached hereto as Exhibit 6. The report required by item 22 above shall be mailed to the Department at the following address:

New Jersey Department of Insurance
Automobile Residual Market Unit
20 West State Street
CN 329
Trenton, New Jersey 08625-0329
Telephone Number: (609) 292-4240
Facsimile Number: (609) 392-0047

If the MDAP requires member companies to provide coverage to eligible persons whose MTF policies expire

during the month of April, 1992, the first member company report would be due July 20, 1992 for the calendar quarter ending June 30, 1992.

24. All costs associated with the administration of this MDAP, as approved by the Commissioner, shall be paid by the member companies that are subject to mandatory assignments. Such costs shall include, but are not limited to, computer time of the MTF servicing carriers; programming costs; cost of computer tapes; reproduction of MTF rate pages; postage and priority mail service. The methodology for apportioning these costs among the member companies subject to mandatory assignments shall be subsequently determined by the Department.

25. The Commissioner reserves the right to make additional assignments pursuant to this MDAP if he determines that the goals of such plan are not being met based on the reports filed by the member companies pursuant to item 22 above.

26. The Commissioner reserves the right to revise the provisions of the MDAP as he deems necessary in order to accomplish the goals of such plan.

27. The Commissioner reserves the right to perform audits, at the expense of the member company, to verify the eligibility determination of the member company pursuant to item 18 above.

(SEAL)

**STATE OF NEW JERSEY
DEPARTMENT OF INSURANCE**

JASPER J JACKSON
DEPUTY COMMISSIONER

P O BOX CN 325
TRENTON 08625
609-292-6812

January 10, 1992

Mr. R. Terry Haskins
Chief Operating Officer
Market Transition Facility
293 Eisenhower Parkway
Livingston, New Jersey 07039

Re: Amendment to the Plan of Operation

Dear Mr. Haskins:

Article V(4), of the MTF Plan of Operation requires a plan to be developed and approved by the Commissioner for the apportionment of profits or losses among the member companies.

I am, therefore, proposing amendments to Article V, Financial and proposing Article XIV, Apportionment of MTF Profits and Losses, to the MFT's Plan of Operation. The amendment to Article V distinguishes the different reporting periods for the purposes of operating results to member companies and for income tax and statutory reporting. Article XIV describes the apportionment plan which is based upon the Aggregate Voluntary Market Industry Quota as defined in Part I of the Plan of Operation.

In view of the fact that some member companies may include the apportionment in their annual statement and

it is imperative to do so now that the companies can prepare their annual statement, I am exercising my right under the Plan of Operation, Article IX(2) (c) to certify this amendment to the members of the Advisory Board. Written comments on the proposal may be sent to the Department by facsimile transmission at (609) 392-0047. I shall certify the proposed amendment to the Plan on January 15, 1992.

Very truly yours,

/s/ Jasper J. Jackson
Jasper J. Jackson
Acting Commissioner

Enclosure

c: Jean Bickal, Regulatory Officer
Donald Bunda, Deputy Attorney General
MTF Advisory Board
